Driving impact in listed assets investments

March 2023

Impact investing is emerging as a powerful way to seek out financial returns while tackling the world's biggest social and environmental challenges.

In this document, we examine AXA IM's approach to impact investing in listed assets.

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Executive Summary

- Impact investing has emerged as a powerful way to seek financial returns while tackling the world's biggest social and environmental challenges. This is framed around the urgent need to deliver on the United Nations' Sustainable Development Goals by 2030

- There is intense debate over how impact investing can be effective when implemented via listed assets. Challenges do remain, such as the low availability of clearly defined key performance indicators and the lack of industry-agreed impact investing standards. However, despite these hurdles we believe that impact investing can be carried out robustly across all listed asset classes, and that we can play a leadership role in influencing an industry common standard

- In this document, we outline AXA IM's approach to impact investing in listed assets. This is the approach adopted by our Core investment teams (Equities, Fixed Income and Multi-Asset)

- We propose two key approaches in equities: Allocating capital to 'impact leaders' and 'impact contributors'; and effecting change in companies through focused investor engagement

- We also detail the framework that drives our investments in green, social and sustainability bonds

Impact investing: A powerful approach

Impact investing aims to be a win-win concept: Investors enjoy potentially attractive financial returns while simultaneously delivering a positive outcome for society and the environment. In simple terms, it's about investing in long-term prosperity for people, and for the planet.

AXA IM launched its first social impact mandate in 1998, investing in small- and mid-cap listed companies in an effort to drive sustainable job creation in France. We now manage impact funds in private investments, green bonds and listed equities, seeking to support solutions that directly address environmental and social issues.[i]

Through impact investing, we want to enhance long-term returns, and aim to achieve this through the allocation of capital to sustainability-related opportunities that target unmet needs in large addressable markets. Alongside this, we aim to drive impact by leveraging our investor rights, to influence companies through engagement.

The roots of impact investing lie in venture capital and private equity, but over recent years the concept has evolved to include the rapidly growing green bonds market, which we will look at in more detail later in this document. And, in turn, as this investment approach moves further into the mainstream, considerable momentum has built around the creation of verifiable impact through investments in publicly listed equities and the wider corporate bond sector. The underlying rationale may be compelling, but doing it in a robust and thoughtful manner is a real challenge.

One key reason the reach of impact investing has widened is the global adoption of the United Nations Sustainable Development Goals (SDGs). Established in 2015 to address challenges including poverty, inequality, climate and health, they have played a vital role in driving the impact agenda. There has been widespread use of the SDGs by a host of stakeholders (governments, businesses, financial institutions and not-for-profit organisations) as a framework to assess those unmet social and environmental needs.

There are 17 SDGs with clearly defined objectives, as well as 169 underlying targets to be met by 2030.

United Nations Sustainable Development Goals (SDGs)

Source: United Nations. For illustrative purposes only.

[i] For Green, Social and Sustainability Bonds: please refer to our specific framework: https://www.axa-im.com/document/4135/view

AXA IM's five pillars for impact investing

At AXA IM, impact investing in listed assets is built on five pillars. These pillars characterise impact investing and differentiate it from other approaches to responsible investing. They drive our approach to equities and form the starting point for our assessment of green, social and sustainability bonds (GSSBs).

1 Intentionality: We consider this a critical element in defining impact investing and a key differentiation point from other approaches to responsible investing. Investments should be made with an upfront objective to achieve a specific positive social or environmental outcome.

Investment managers must have the intention to create impact through the allocation of capital to companies that generate, or have scope to generate, meaningful positive outcomes via their business activities. Therefore, a portfolio should have a clear identity that targets social or environmental goals. Our research then seeks to identify companies that demonstrate intentional, strategic commitment to positive impact in those areas.
The investment managers can also use their influence as investors to pursue active engagement with companies and seek to generate impact through change.

2 Materiality: Many companies generate positive outcomes for society and the environment. However, not all impact is equal. Our position is to invest in companies where the positive outcomes are of material significance to the beneficiaries, the company, or to both. Ideally, a firm's initiatives should be of strategic importance and make up a material proportion of the company's overall commercial activities (what might be deemed 'pure plays'). However, there is also room for companies that are an important part of a solution, and so may affect significant change through a smaller part of their overall activities (what might be deemed 'decisive plays').

We pay attention to the proportion of a company's revenues that align with the SDGs. Importantly though, we will also consider a variety of other factors, such as the severity of the issue being addressed, the number of beneficiaries (particularly currently underserved people), or the extent to which a firm is a leading solutions provider relative to its peers. To help us compare materiality across companies we will consider the level of impact generated against the size of the investment being made, and the scale of the business e.g. relative to market capitalisation or corporate revenues.

3 Additionality: This is an idea that originated in the philanthropic not-for-profit sector, where donations were allocated based on likelihood they could help resolve unmet environmental and social needs. Additionality – particularly whether it is possible in a listed asset context – has been a focus of much debate.

We principally focus on the extent to which a company is making its 'needed' products and services more accessible or commercially viable, for example through innovation and new technologies, lower prices, or better distribution. Such commercial strategies, if done profitably, can create long-term competitive advantages for those firms best able to exploit opportunities in satisfying unmet needs across potentially huge addressable markets. Importantly, we also assess the extent to which corporate practices, behaviour and operations are filling a void in terms of leading, influencing and shaping others' approaches.

4 Negative externality: A company's corporate practices, or products and services, may significantly undermine the positive impact it is generating elsewhere. For example, this could include involvement in controversies or the extensive use of coal in business activities. It is important that negative externalities, and a firm's commitment to address them, are fully considered alongside positive outcomes.

5 Measurability: There needs to be a clear methodology and commitment to measuring and reporting the social and environmental performance of investments. These need to be monitored over time. Impact is more difficult to measure than environmental, social and governance (ESG) factors because of the lower degree of data availability and standardisation. This also includes collating and checking the integrity of publicly available data and third-party research.

Impact investing: How we assess companies

We are determined to ensure our research processes have a strong foundation and that they can stand up to scrutiny. We fundamentally believe that there is no substitute for sustained, in-depth analysis and hard work. We do not want to be reliant solely on third-party research methodologies and scores, but instead, to be a proactive and sceptical handler of data analysis and information.

We believe our methods for impact investing are distinct from our other approaches to responsible investment. Nevertheless, we do harness our broader techniques for integrating ESG factors in our impact investment processes. This includes systematically incorporating an assessment of material ESG-related risks and opportunities into our analysis. We also comply with AXA IM's ESG Standards Policy. This may involve excluding companies involved in certain industrial activities, such as the production of controversial weapons, or which are the subject of major controversies and breaches of international norms.

We approach impact investing through the themes outlined in the following table. These cover what we see as major global challenges or important solutions. We have identified a sub-set of the SDGs that we believe are being addressed through these investment themes. AXA IM's approach to impact investing has been established with the purpose of delivering attractive financial returns, while also promoting positive change around key global challenges. Our impact research framework is built to identify the companies that can achieve these goals. While this applies most explicitly to impact equities, the same priorities inform our work on GSSBs which is discussed in more detail later in the document.

We believe our own impact qualitative assessment is essential to ensuring the effectiveness of an impact strategy. Our dedicated impact analysts conduct their own impact research on companies. Portfolio managers use these assessments to build their impact portfolios. We have also established a 'theme pod' structure led by portfolio managers who are experts on certain impact areas. Theme pod meetings are forums where industry and thematic trends are discussed. They also help identify potential impact investment opportunities.

Our impact investing themes and links to the SDGs

Prosperity for people		Prosperity for the planet	
Empowerment		**Energy Transition**	
Education and Entrepreneurship	Human Capital and Diversity	Smart Energy	Low-Carbon Transport
Health & Wellbeing		**Sustainable Industry**	
Wellbeing and Safety	Healthcare Solutions	Sustainable Production	Agriculture and Sustainable Food
Inclusion		**Resource Scarcity**	
Financial and Digital Inclusion	Housing and Essential Infrastructure	Recycling and Waste Reduction	Water

In our equities methodology, we aim to identify and track a range of company-relevant impact metrics or key performance indicators (KPIs), across five categories:

1. Products and services
2. Research and development
3. Operations
4. Corporate social responsibility (CSR) initiatives
5. Negative externalities

Tracking these KPIs allows us to judge the social and environmental contributions of companies and their progression. As a result, we feel we are better equipped to judge which businesses are aligned with certain SDGs, and by how much. KPI monitoring also helps highlight disclosure gaps at companies. When this tracking is done across a breadth of firms within a sector or impact theme, it also helps us to make comparisons and to see obvious areas for improvement. Accordingly, we can thoughtfully engage with companies around these disclosure gaps and highlight areas for improvement.

We believe our in-depth impact analysis, when integrated into our traditional company and financial analysis, is a powerful tool which can help us identify potential long-term winners. These are the companies that we think can enjoy a self-reinforcing relationship between generating outstanding sustainability and financial outcomes. Not all companies can achieve this, and we want to be invested in the ones that can.

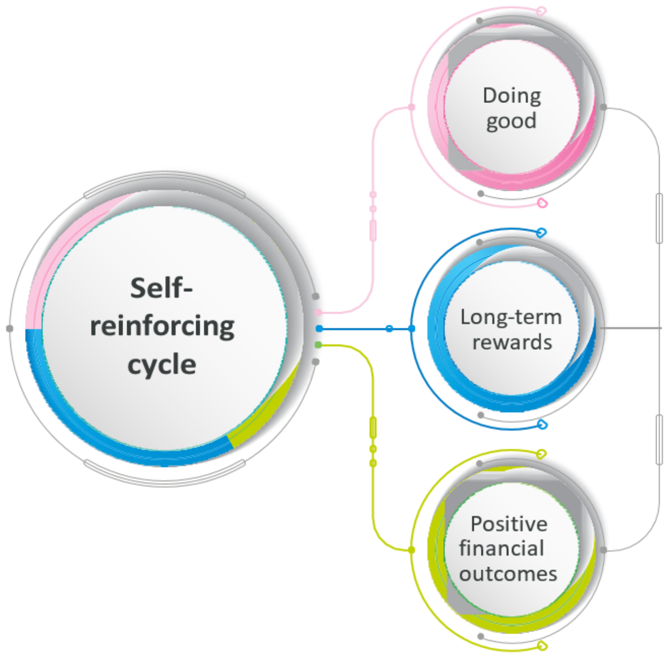
Below we outline some of these KPIs. Each is tracked, where possible, against company targets. On the following page we outline how we see the potential link between impact and returns.

KPI examples by theme

Theme	Typical KPI	Primary SDG
Smart energy	Renewable energy generated Avoided greenhouse gas emissions	
Water Housing & essential infrastructure	Volume of water saved People with new access to clean water and sanitation	
Healthcare solutions	Number of treated patients	
Human capital & diversity Education and entrepreneurship Financial and digital inclusion	Women in management and on the board of directors Young people gaining vocational training Share of micro finance loans	

Source: AXA Investment Managers. For illustrative purposes only.

The relationship between impact and financial returns



- An intent and ability to contribute towards the SDGS

  Operating in industries and countries where impact is maximised

  Doing extra – lower cost, better access, Corporate Social Responsibility programmes

- Brand and stakeholder loyalties

  Early mover into potentially huge addressable market

  Creating competitive advantage through innovation & efficiency, low prices, and high customer touch

- Strong intangible value to help sustain margins and profitability

  Exposure to secular growth trends

  Risk Mitigation

  Strong financial returns, and ability to reinvest into more impactful solutions

Source: AXA Investment Managers. For illustrative purposes only.

How we identify impact companies

Through our research, we identify companies that may deliver verifiable impact in two categories: Impact leaders; and impact contributors. This applies most directly to equity investments, with specific GSSB approaches examined in detail on the following pages.

Impact Leaders are the highest rated in terms of generating positive societal impact, in the present and the future. Impact investors have traditionally focused on companies that generate positive outcomes through the provision of their goods and services (products and services impact leaders). This is also where we focus most of our research. However, we are of the conviction that there is also a place within the impact landscape for exceptional companies bringing about positive change through their corporate practices, behaviour and operations (*operational impact leaders*).

Products and services impact leaders are firms that sell goods and services of critical importance and which generate significant 'additionality' by leveraging technology, scale or innovation to make goods and services accessible and commercially viable in potentially underserved markets. Such firms should be able to create a competitive advantage as they establish leading positions in new growth markets.

Our expectation is that operational impact leaders cannot simply be good corporate citizens but must also aim to drive broader change through their corporate behaviour and practices. This would include companies with best-in-class approaches globally, but also those where practices are leading and shaping a country or a sector. Issues addressed may relate to supply chain management, or to empowering women in the workplace etc. We would need clear evidence that a firm is indeed best-in-class, is setting genuinely ambitious operational targets, is vocally highlighting issues, is pioneering solutions through leadership or collaboration with peers, or is affecting the lives of many beneficiaries. This is how we address the additionality test.

Impact leaders will have a clear strategic intention – as articulated by the board and senior management – to contribute to society and the environment while also aiming to generate healthy financial returns. They should be able to clearly articulate how those contributions are also benefiting the business and its investors. This can be through stronger brands, increased loyalty from key stakeholders, or increased preparedness for a resource-constrained future.

Impact leaders should be able to satisfy our materiality test. They need to generate significant positive impact through a large portion of their business activities (i.e. pure plays) or address critical issues for a notable group of beneficiaries through a smaller part of their business (i.e. decisive plays). Such firms can vary between front-line activities (e.g. renewable energy generation), to enabling activities that are embedded within a supply chain and offer important services or technologies. Impact leaders can tackle a single SDG or multiple SDGs.

Impact leader status is awarded only to the leading companies, though this does not mean that such companies are perfect or without fault. There are no guarantees that they will be able to keep this rating over time. We will monitor the progress of such companies and engage with them to ensure that they remain leaders.

Impact contributors, meanwhile, are companies that verifiably generate significant positive social or environmental impact but have not obtained the impact leader status due to considerations that may include impact theme alignment exposure – perhaps only a limited portion of revenue contributes to the SDGs while the rest of the business is largely neutral. They may also be held back by the relative severity of the issue being addressed, a lack of corroborating disclosures, or negative externalities.

Our framework for investing in Green, Social and Sustainability (GSSB) Bonds

The processes detailed above feed into the way we assess companies issuing GSSBs. However, we have also developed a focused framework to help us decide on the viability of issuance in this space. The approach is built on four straightforward pillars.

1. The environmental, social and governance (ESG) quality and strategy of the issuer
2. The use of proceeds and the process for project selection
3. The management of proceeds
4. Impact reporting

For each pillar, our analysts review, assess and monitor several well-defined criteria, many of which are mandatory. At the very least, the issuer has to surpass our exclusion criteria and to comply with our "requirement" criteria in order to be investable.

If a GSSB also meets our "expectation" criteria, it would place the issuer among the GSSB leaders, in our view. The factors outlined below are intended to be indicative and non-exhaustive. This is primarily due to the fact that individual GSSBs can vary greatly and therefore their individual assessment involves subjective criteria, as is always the case in qualitative analyses.

At AXA IM, we believe that the use of proceeds of a green bond should reflect the issuer's efforts towards improving its overall environmental strategy and its alignment with the Paris Agreement on climate change. On the social side, the issuer should also make its ambition to deliver positive societal outcomes clear. Full transparency about the projects financed and on the tracking of the proceeds is therefore essential to our assessment. We pay particular attention to impact reporting, where both qualitative and quantitative indicators are expected.

Pillar 1: ESG quality and strategy of the issuer

Our first pillar is the one that makes AXA IM's approach different from the Green Bond Principles. Within the Principles, it is not considered as a fully-fledged pillar. By considering both the ESG quality and strategy of the issuer, our assessment aims to avoid 'greenwashing' – what could be perceived as green bonds issued for public relations reasons.

The ESG quality is considered according to AXA IM's proprietary ESG scores as well as the issuer's exposure to controversies. We want to ensure that the issuer demonstrates minimum ESG commitments and properly manages environmental and social risks.

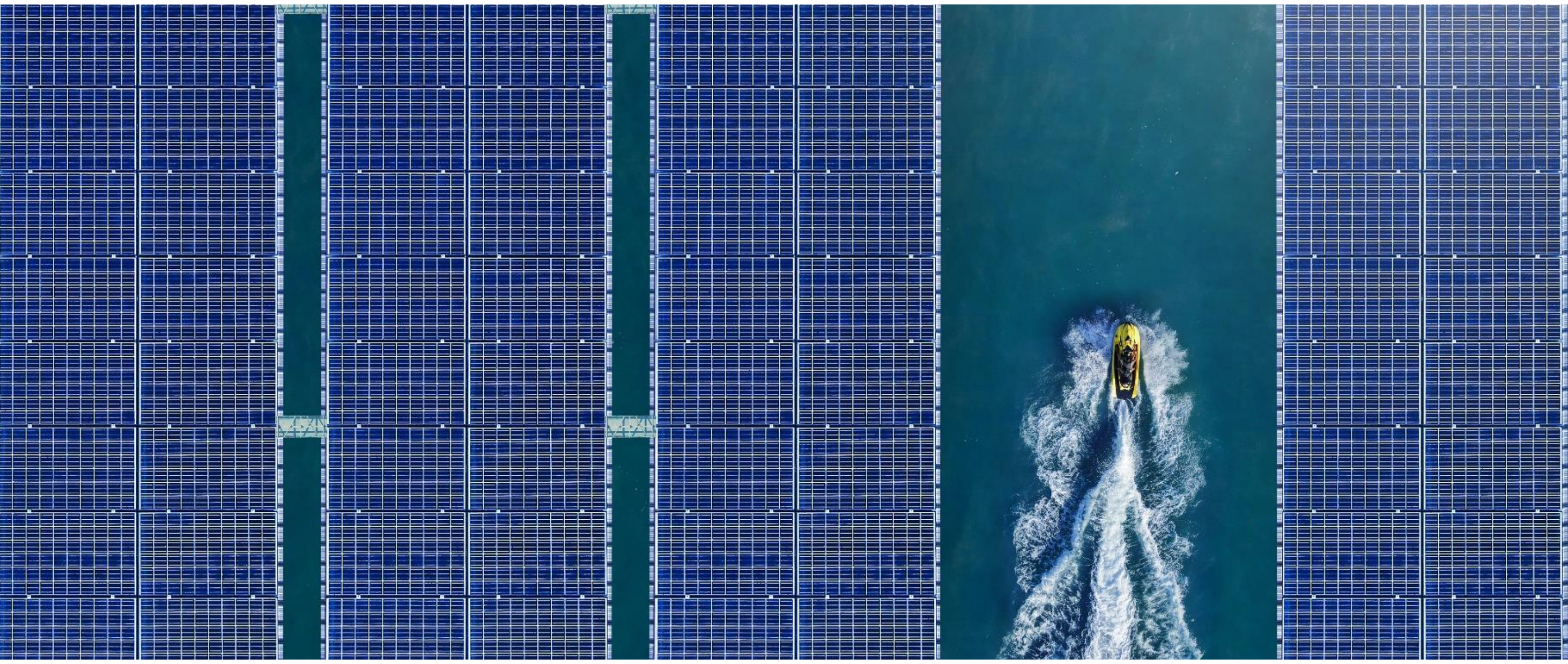
The environmental strategy refers to a forward-looking approach. The aim here is to evaluate whether the green bond fits into the issuer's environmental short- and long-term objectives. Green bond issuers should clearly exhibit a senior management and board-level commitment to align wider commercial strategy and activities with helping meet the COP21 Paris Agreement goals. We also expect green bond issuers to take action in order to align their business models with a global warming scenario below 2°C. An overall coherence between the environmental strategy and the green bond issuance is necessary.

Pillar 1: For social bonds

The assessment process for social bonds is similar, except for expectations. We want to ensure consistency between the social bond and the issuer's social strategy to avoid any opportunistic-only issuance that wouldn't lead to a lasting change. We also want to be assured the issuance is not only a public relation exercise.

GSSB pillar 1 breakdown

Requirement	Expectation	Exclusion criteria
▸ Clear definition of the issuer's environmental strategy and commitments ▸ Alignment of the green bond with its sustainability policies and processes	▸ Quantified short- and long-term environmental targets	▸ Weak ESG score ▸ Severe controversy



Pillar 2: The use of proceeds and the process for project selection

Our second pillar focuses on how the proceeds of a green bond are used. It merges the first two pillars of the Green Bond Principles. Our aim here is to control the quality of the eligible projects by understanding the selection process and the eligibility criteria. More importantly, we focus on projects or assets delivering additionality and impact. Our process rewards projects that are innovative, impactful and going beyond the issuer's "business as usual". AXA IM's green taxonomy is based on technical criteria from the EU Taxonomy and the Climate Bonds Initiative to ensure alignment with the Greenfin Label requirements.

Pillar 2 for social bonds

There are no specific exclusion criteria for our social bonds investments up to now. On the breakdown of the proceeds per project, we can be more flexible as our experience shows issuers are often not in a position to give any indicative split before the first anniversary of the social bond issuance.

The additionality aspect is key but poorly reported in the social bond market. While this is not a requirement, issuers who can justify the additionality of their social projects are viewed more favourably.

We nevertheless expect social bond issuers to apply relevant and robust criteria to define the target populations and areas that they aim to support through funded projects. This is very important to ensure that we will finance impactful social projects.

GSSB pillar 2 breakdown

Requirement	Expectation	Exclusion criteria
▸ Clear description of the eligible assets and the category they belong to ▸ Compliance with AXA IM's taxonomy ▸ Disclosure of the eligibility criteria for each category of eligible projects ▸ (At least) indicative or expected breakdown of the proceeds allocation to the eligible projects ▸ Disclosure of the process used to select and evaluate the eligible projects	▸ Description of how environmental and social risks and potential rebound effects related to the eligible projects are taken into consideration ▸ Estimated share of financing new assets versus refinancing existing assets, plus look-back period for existing assets ▸ Establish a qualified and diversified internal committee to select green projects ▸ Description of how eligible projects bring additionality (e.g. through financial incentives applied to green assets	▸ Any project related to fossil fuel or nuclear energy production, regardless of where it stands in the value chain ▸ Large new hydropower projects

Pillar 3: The management of proceeds

Our third pillar, similarly to the third of the Green Bond Principles, relates to the management of proceeds. It aims to verify that the issuer has sufficient guarantees in place to control the allocation of proceeds to eligible projects. We are looking to ensure that the green bond proceeds will effectively finance eligible projects.

Pillar 3 for social bonds:
The assessment process for social bonds is the same.

GSSB pillar 3 breakdown

Requirement	Expectation
▸ Description and transparency of the internal process used to track the proceeds	▸ External/independent verification of the proceeds allocation ▸ Segregation of the green bond proceeds in a separated account or portfolio

Pillar 4: Impact reporting

Our fourth pillar, also similar to the Green Bond Principles, focuses on reporting. While the principles only encourage issuers to provide impact indicators, it is a mandatory criterion within our assessment process. It allows us to measure our positive impact and the environmental benefits of our green bond investments.

Pillar 4 for social bonds:

The assessment process for social bonds is similar. We are particularly sensitive to the quality and clarity of impact reporting, which we know is more challenging in the social bond market. As impact reporting in the green bond market matures and improves, we are also encouraging green bond issuers to enrich their impact reporting with social KPIs when doable (e.g. when green projects have a positive social impact on surrounding communities). Of note, we can downgrade our opinion if we notice a breach in comparison to what was announced at the time of issuance.

GSSB pillar 4 breakdown

Requirement	Expectation	Exclusion criteria
▸ Allocation report to eligible categories, and balance of unallocated proceeds ▸ Provide relevant qualitative and quantitative key performance indicators (KPIs), at least for each eligible category ▸ Disclose details on the methodology, assumptions and baselines used to calculate the impact	▸ Rely on an independent third party in the calculation of the environmental impact ▸ Provide KPIs on a line by line basis	▸ No publication of an impact report

How we engage companies on the United Nations' Sustainable Development Goals

Engagement is an important route for investors to drive impact in listed assets – public equities and corporate bonds in particular. When done right, intervention by investors can help achieve broader goals such as the UN SDGs.

We believe engagement is a powerful way to change corporate practices and influence decision making. The proactive and effective use of investor rights and responsibilities is particularly relevant within the scope of the SDGs, where significant and rapid change is required. Governments and supranational bodies will provide momentum, but cannot be expected to lift the burden or effectively coordinate efforts alone.

The listed corporate universe is clearly a vital agent for change. We estimate that listed equities globally represent approximately $67trn of market capitalisation.[ii] We consider engagement to principally be a tool for effecting change through this vast economic powerbase. Key areas of potential engagement include:

Products and Services: Encouraging companies to accelerate the shift towards solutions that contribute more efficiently to social and environmental issues. This comprises encouraging the commercial uptake of new and innovative solutions, and a move away from products and/or solutions that are traditionally associated with negative externalities.

Operations: Encouraging companies to implement sounder operational practices, to continuously improve their operational footprint and/or to enhance employer-employee relationships. Traditionally viewed from a risk-mitigation perspective, we think operational footprint optimisation can also prove an opportunity to generate positive impact, notably as we consider products' and/or solutions' lifecycle emissions and impacts.

Board and management accountability: Establishing clear expectations of board directors and senior executives about their capacity to assess and profit from commercial opportunities related to the SDGs. This includes ensuring the right expertise on the board and the appropriate board-level processes and structures to ensure that new commercial opportunities related to impact can be identified.

Transparency: Calling for transparency from companies around their strategic decision-making processes and capital allocation to commercial activities related to the SDGs. We are also pressing for this information to be disclosed publicly either in a report or verbally. We will question the extent to which a firm's SDG contributions are genuine and aligned with its broader corporate strategy.

Measurement: Requesting details on internal methodologies that firms use to assess, on an ex-ante basis, the potential impact and additionality from their capital allocation to impact-related opportunities. This should lead to a framework which companies can implement to measure key performance indicators on an ex-post basis.

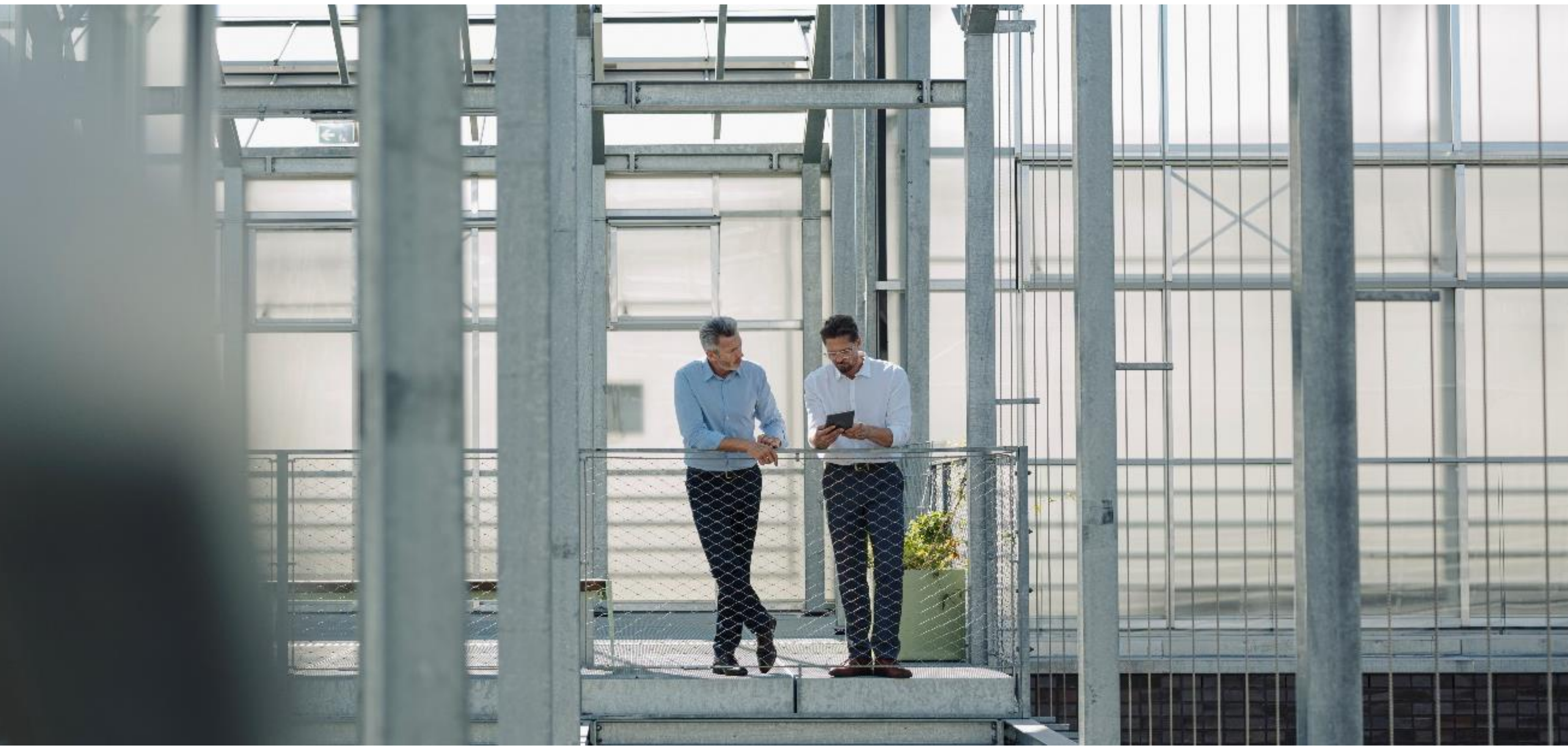
Reporting: Asking for the implementation of regular reporting on impact and SDG-related metrics.

[ii] Source: FactSet, AXA Investment Managers, Sept. 2022

We believe that these targets are sufficiently ambitious and consider them to be long-term engagement objectives. Currently very few (if any) companies globally are close to fulfilling all these engagement-related objectives.

Separately, we will also continue our involvement in appropriate industry initiatives for collaborative engagement and public policy-related dialogue. We also collaborate with other global financial institutions to overcome some of the broader challenges of impact investing in listed assets. One of these obstacles includes the lack of industry-agreed impact investing standards and frameworks. AXA IM is a member of the Principles for Responsible Investment and the Global Impact Investing Network. We sit on the investor council for the latter.

We also are long-running participants in a broad range of working groups and public policy consultations. For example, this includes supporting the Task Force on Climate Related Financial Disclosures and providing feedback to the European Commission's taxonomy for environmentally sustainable economic activities.[iii]



Mapping our GSSB investments with the SDGs

The high level of transparency that we expect from the GSSBs in which we invest allows us to know what type of green and social activities we fund, and align them with the SDGs. There is no consensus on the way to approach SDGs in the GSSB market. We therefore built our own methodology to map the SDGs against our GSSB taxonomy. We distinguish between the green and social activities that directly contribute to some of the SDGs, and those that only align with it.

An illustrative example of the kind of mapping we carry out is shown on the following page. We aim to measure our contribution to the SDGs through our GSSB investments. We also pay great attention to doing "no harm" to some SDGs while helping achieve others. To ensure that, we rely on the two first pillars of our assessment framework – the ESG quality and sustainability strategy of the issuer, and the use of proceeds and process for project selection.

[iii] Task Force on Climate Related Financial Disclosures Supporters

Environmental Projects / SDGs	1	2	3	6	7	8	9	11	12	13	14	15
Renewable Energies			✓ A		✓ D	✓ D	✓ A	✓ A		✓ A		
Energy Efficiency					✓ D	✓ D	✓ D	✓ A		✓ A		
Green Buildings								✓ D		✓ A		
Low-Carbon Transportation			✓ A				✓ A	✓ D		✓ A		
Water Management				✓ D				✓ A	✓ D		✓ D	✓ A
Waste Management				✓ A		✓ A		✓ D	✓ D		✓ A	
Sustainable Land Use			✓ A						✓ D		✓ A	✓ D
Adaptation Infrastructure	✓ A	✓ D					✓ D	✓ A		✓ D		
Biodiversity Conservation		✓ A		✓ D							✓ D	✓ D

✓ Direct Impact ✓ Alignment

Source: AXA IM and United Nations

	Social Projects / SDGs	1	2	3	4	5	6	7	8	9	10	11
	Affordable Basic Infrastructure						✓ D			✓ D		✓ A
	Access to Financial Services	✓ D							✓ A		✓ A	
	Access to Education	✓ A			✓ D				✓ D		✓ A	
	Access to Energy	✓ A						✓ D			✓ A	
	Access to Healthcare	✓ A		✓ D							✓ A	
	Access to Telecommunications	✓ A								✓ D	✓ A	
	Affordable Housing	✓ A									✓ A	✓ D
Employment Generation	Microfinance	✓ D										
Employment Generation	SMEs Financing								✓ D	✓ A		
	Food Security/ Sustainable Farming		✓ D									
	Socioeconomic Empowerment	✓ D									✓ D	
	Women Empowerment					✓ D					✓ D	

✓ Direct Impact ✓ Alignment

Source: AXA IM and United Nations

Q&A: Answering the big questions

Is there a trade-off between impact and financial returns?

We believe there can be a trade-off when companies implement strategies with a short-term mindset, by looking for temporary uplift in financial returns or social and environmental impact. For example, customers, suppliers or other stakeholders may suffer should companies seek to squeeze an extra few cents of earnings per share out of the current year, or margins may suffer when offering a one-off or isolated product give-away.

When an intent to create positive impact is genuine and embedded into a company's offerings and practices, then we believe this promotes better corporate health. It can also potentially lead to improved long-term returns for investors.

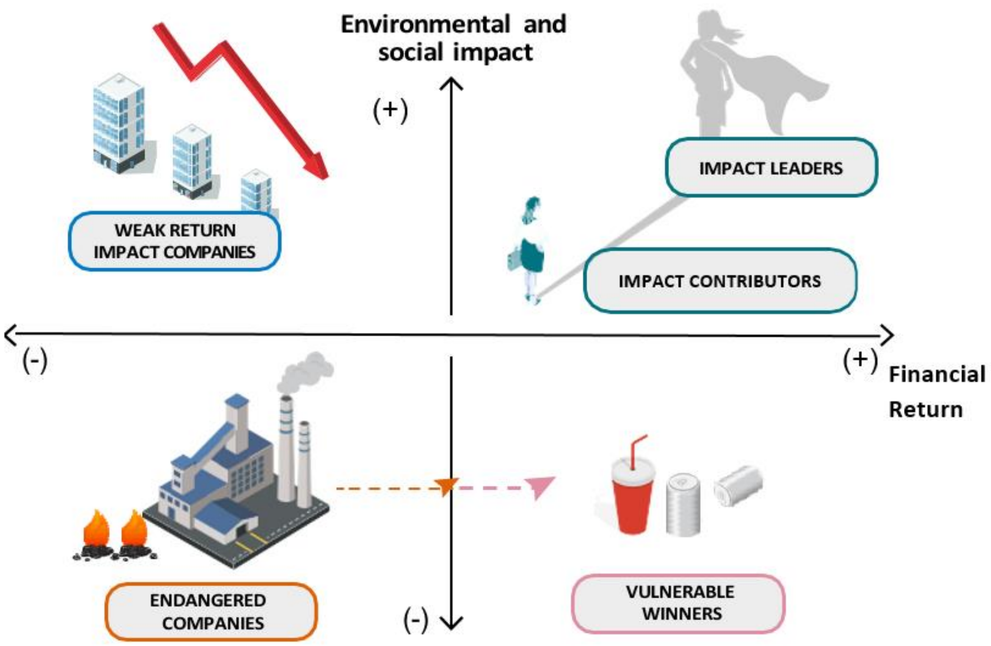
Companies that can profitably contribute towards the SDGs are not only helping society and the environment, but we think they also give themselves a better chance at being among the long-term winners by:

- Focusing on the SDGs and addressing unmet needs – they are more likely to be first movers into potentially large addressable markets
- Pioneering accessibility for their products and services – they can establish significant competitive advantages for their business
- Promoting solutions and acting responsibly – they are creating important loyalties among key stakeholders and are better preparing their business for a resource–constrained future.

Of course, many companies will never achieve this self-reinforcing impact and returns cycle. This may be due to the quality of management, poor oversight of the board, or the industry that they operate within. Some positively impactful industries are commoditised, highly competitive and/or capital intensive. Government influences can exacerbate these pressures by distorting capital allocation incentives.

The graphic below shows the spectrum of companies as we currently see it. The impact leaders in the top right quadrant are those that have best established positive causation and correlation between impact and returns. We aim to set up our research in a way that helps us identify these companies.

The spectrum of companies



Source: AXA Investment Managers. For illustrative purposes only.

What role can third-party data providers play in establishing impact company universes?

Third-party research companies and index providers can offer a range of valuable datasets on impact and many have gone about creating impact company universes in different ways.

Some are taking a straightforward approach of using sector-based criteria by mapping certain SDGs to industries. Others are using databases of revenue composition of companies. Some types of revenue are put in 'positive' impact buckets (e.g. renewable energy generation or healthcare services) and others in 'negative' revenue buckets (e.g. sugary snacks or drinks). The datasets that these firms provide, once their integrity has been established, can be insightful and powerful tools for asset managers. We can use them to help identify opportunities, as an extra input in our company assessments, and to help us with reporting. The datasets will improve over time, and methodologies used by these businesses will become more sophisticated.

However, the subjective nature of what constitutes an impact company makes it difficult to systemise impact assessments across a broad range of thousands of companies. The difficulty is heightened when you consider the lack of standardised impact disclosures across many companies. Even with better disclosure it will still be the case that the most appropriate set of impact KPIs to judge one company may be completely different for another, even for two firms operating in the same industry. For example, some pharmaceutical companies should be judged on their drug pricing policies, while others should be assessed on the quality or focus of their research and development. Others should be judged on their policies to drive broader access to medicines to more beneficiaries.

AXA IM's approach relies on in-depth analysis of businesses. We use data from third parties and can leverage the information that this provides in relation to company revenue compositions, as well as ESG scores and assessments. However, we also consider many other factors. These include: The severity of the issue being addressed; the number of beneficiaries being positively affected; the extent to which beneficiaries are currently underserved; and a company's additionality in driving down prices or improving accessibility for their needed products. We also consider how a company's actions in turn affect the behaviour of competitors or the industry at large.

To do this effectively it is important to rigorously track KPIs and company behaviour within a focused list of companies.

The ambiguities around what constitutes an impact company or fund are unlikely to be resolved anytime soon. As such, it will be a challenge to establish credible and widely-acknowledged universes or indices of impact companies. Therefore, impact investment asset managers need to maintain high levels of transparency with clients, to justify their portfolio decisions, and to collaborate with peers to establish and adhere to best practices.

How should impact investors deal with poor and inconsistent disclosures of impact-related performance indicators by companies?

A lot of discussion around impact investment focuses on the availability, or lack, of backward-looking performance measures. There is no doubt these can represent important evidence of past actions and offer signs of how a firm has genuinely performed against promises. However, good disclosure alone does not resolve global issues around climate change, water scarcity or lack of healthcare provision.

We recognise that there are differing expectations in local markets with regards to transparency and some companies, as a result, may not be leaders in disclosure from a global standard. Sometimes these are due to reasons around commercially sensitive data, evolving internal measurement methodologies or the disclosure burden for smaller companies. Accordingly, we do not believe that disclosure alone should be an impediment to investing in firms which can otherwise be assessed to be impact leaders.

Nonetheless, we still expect the following from impact leaders:

- A clear willingness to implement the monitoring and disclosure of relevant impact-related performance data, with an understanding of their links to the SDGs. This is a good sign of a company management's intent to generate positive outcomes for society. Management teams need to understand what contributions – both positive and negative – their companies are making, and what more they can do to improve performance.

- An understanding from management teams that strong practices around disclosure can influence disclosure practices across the broader corporate landscape. They should understand the rationale behind establishing ambitious and stretched targets
- An openness to engage with investors on this issue and responding positively to recommendations for better disclosure.

We also recognise that impact investors need to be accountable to their clients. This requires a clear system for measuring whatever useful data is available, and a commitment to encourage better disclosures from portfolio companies. Leading investors in this field have an important role in shaping the future of this industry. The current absence of standards and frameworks as well as the scarcity of impact data is an issue which affects all financial industry participants.

Are impact investments very similar to emerging and frontier market strategies?

Many of the SDGs have a clear focus on targeting challenges for low-income countries. SDGs 1, 2 and 10 are focused on eradicating poverty, hunger and inequality while others seek to improve access for poorer people to basic infrastructure and services (SDGs 3, 4, 6, 7, 9).

The UN Conference on Trade and Development World Investment Report for 2014 estimated that an annual \$5trn-\$7trn investment would be required to meet the SDG 2030 goals. Approximately two-thirds of this would need to be invested into the developing world. Hence it is not surprising that the 169 underlying targets of the SDGs have a clear focus on meeting the economic development challenges in low-income countries.

Emerging market listed companies represent around 11% of the MSCI All Country World Index (MSCI ACWI). However, it is worth noting that investing in developing market listed companies is not the only way to have exposure to business activities in low-income countries. Presently, nearly 27% of the revenue from all MSCI ACWI listed firms is earned in emerging markets.

It is also important to note that there are global benefits from the advancement of solutions that address chronic health issues, climate change and resource scarcity – whether they come from a developed or emerging market company.

Many of the SDGs and targets do not appear investible. How do you deal with this?

Many of the SDGs can be easily addressed directly by listed companies through the provision of goods and services – for example SDG 3 – “ensure healthy lives and promote well-being for all at all ages”. Other SDGs are more likely to be addressed indirectly or as a result of company activities. For example, SDG 10 – “reduce inequality within and among countries”.

When you delve into the targets it is apparent that it is difficult to align many of them with the activities of listed companies. Some targets are very broad, such as SDG target 1.1 – to eradicate poverty for all people everywhere by 2030. Some targets may need to be facilitated by governments rather than companies, for example target 5.2 – eliminate all forms of violence against all women and girls in the public and private spheres. Target 16.3, meanwhile, calls on authorities to promote the rule of law at national and international levels and ensure equal access to justice for all.

Our assessment is that about 50 of the sub-targets can be directly addressed by investment-related activities. Other targets might be better addressed by governments and other stakeholders such as not-for-profit organisations.

The important point is that the alignment or mapping of company activities with the SDGs cannot be treated as an exact science. The SDGs are very broad and hence very adaptable to a changing world. However, despite there being 17 goals and 169 targets, not every important global need could have been foreseen or covered by the framework.

Accordingly, some flexibility and creative licence is required when targeting the SDGs through investment. We recommend that investors use the SDG targets that fit best, rather than fit exactly. If there are no targets that can serve a purpose, then investors should be guided by the overarching aims of the SDG in question. Companies that can visibly deliver SDG solutions as a by-product of their activities should not be ruled out. A perfect taxonomy should not be the enemy of a good outcome.

To what extent should negative externalities rule out companies as candidates for inclusion in an impact portfolio?

Negative externalities should be considered for all investments. It is very difficult to reconcile net positive and negative outcomes, especially in what may be very different areas. For example, how do we weigh the fact that a business may be driving adoption of insect repellent use in India but may also be reliant on palm oil in its production? How do we assess a healthcare business that is rolling out a new cure for a disease at a price point that may lower the overall cost burden to society, but that nevertheless appears unjustifiably high in the public consciousness? The electric vehicle (EV) industry is fraught with debate given the reliance on exhaustible raw materials, though the end goal is clearly worth striving for – better technologies, powered by renewable energy, increased equipment standardisation and recycling.

We believe that the full assessment of net social and environmental outcomes cannot be achieved through an equation. It is a matter of judgement. Arriving at opinions and verdicts need to be backed by data and be well documented. Negative externalities clearly need to be analysed for all companies.

Which listed asset funds deserve an impact label, and which funds don't?

We have outlined what we believe are the five fundamental pillars of what constitutes a listed asset impact strategy (see page 5). We also believe that while this framework is demanding, it provides sufficient space for the broad church of views around how positive societal change can be galvanised through an investment strategy.

Some strategies will prioritise investment into impact leaders, where positive change will likely continue to accrue because of a company's existing model. Others will prioritise investing and engaging with companies where significant positive change can materialise as firms' strategies change – and where investor-led additionality is easier to demonstrate.

Some strategies may focus more on a company's operations (e.g. related to human capital management) than on products and services. Such impact strategies may distinguish themselves from other responsible investment funds because of the clearer identity of the fund in promoting positive change around specific issues. We believe, with such portfolios, that the fund manager should consider whether the portfolio companies are providing leadership with respect to the identified issues and solutions.

Regardless of the nuances between different listed asset impact strategies, we believe that an impact fund will be on firm ground if it can clearly demonstrate adherence to our five pillars and provide sufficient reporting transparency.

Those looking to allocate capital into listed impact strategies should hopefully find our five pillars as a useful guide to differentiate between asset managers. Other considerations will also be of critical importance, including the commitment of the asset management organisation to responsible investing and the track record of the fund manager at delivering best-in-class investment solutions against client needs and guidelines.

For further information on AXA IM's approach to responsible investing and impacting investing please visit **www.axa-im.com/en/responsible-investing** or contact your local sales representative.