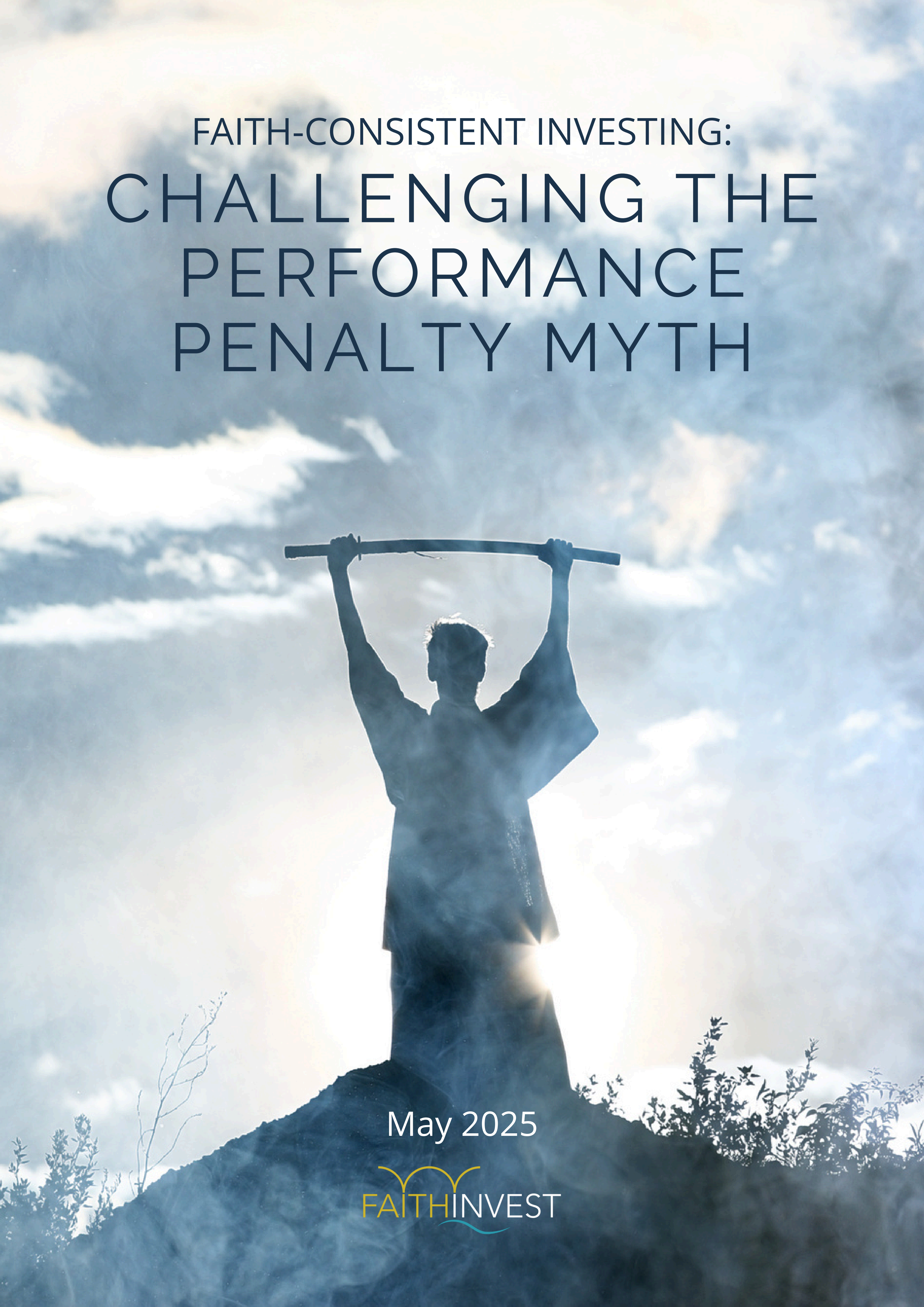
FAITH-CONSISTENT INVESTING:

CHALLENGING THE PERFORMANCE PENALTY MYTH



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FAITHINVEST

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EXECUTIVE
SUMMARY

Faith organisations face a significant dilemma: while they recognise the moral imperative to align their investments with their beliefs, many hesitate to fully embrace faith-consistent investing (FCI) due to concerns about sacrificing financial returns.

This perceived trade-off between values and performance has created a significant disconnect between institutional missions and investment practices across the faith community. This paper discusses how the alignment of financial investments with religious values can produce competitive returns while promoting positive societal and environmental outcomes.

Drawing on the perspectives of investment professionals at FaithInvest with extensive experience in faith-based and asset management organisations, the paper challenges the common misconception that investing according to faith principles, or values principles more broadly, necessarily results in diminished financial performance.

Instead, it argues that FCI – when thoughtfully implemented – can lead to improved investment outcomes by addressing systemic risks that traditional investment approaches often overlook.

INTRODUCTION

The journey toward faith-consistent investing

The integration of faith values with investment decisions represents a meaningful opportunity for religious organisations to extend their mission beyond traditional charitable activities to include their investable assets. Faith-consistent investing (FCI) enables faith-based asset owners to align their investments with their core beliefs while maintaining their fiduciary responsibilities to act in the best interests of their clients, including producing the financial returns they seek.

Faith investments occupy a distinctive space in the investment landscape—neither purely public nor private but representing what might be called the 'Third Sector'—i.e.,mission-oriented organisations that invest for communities and for broader societal good alongside financial returns. This unique positioning allows faith-based investors to bridge market gaps and pursue holistic outcomes that traditional investment approaches might overlook.

This sentiment encapsulates the essence of FCI—recognising that financial returns and faith values need not be in opposition but can instead be mutually reinforcing.

Since our establishment in 2019, FaithInvest has developed a comprehensive understanding of the concerns and challenges faith-based investors experience and face. As a mission-oriented organisation, we support faith-based investors in their efforts, and part of that support is helping to demystify misconceptions about FCI and address concerns about the financial implications of aligning investments with values.

FAITH & PERFORMANCE

Addressing the trade-off myth

A persistent myth in investment management suggests that FCI inherently results in suboptimal investment returns. This belief often stems from the assumption that limiting the investment universe based on faith principles will lead to missed opportunities or increased risk due to reduced diversification. This misconception can lead faith-based asset owners to hesitate in fully aligning their investments with their values, potentially creating a disconnect between their mission and their financial practices.

However, this perspective takes a narrow, short-term view that fails to account for the complex realities of today's global economy and the evolving nature of investment risks and opportunities. As Dave Zellner, Executive Chair of FaithInvest and former Chief Investment Officer at Wespath Benefits and Investments argues: 'By taking a holistic, long-term view that considers systemic risks and opportunities, FCI can not only align with investors' values but also potentially enhance long-term financial performance.'

In this context, 'long-term' refers to investment horizons that extend well beyond the typical 1- to 3-year measurement periods common in the industry. For faith-based investors—particularly those serving endowments, foundations, and pension funds—appropriate timeframes often span decades rather than years, aligning with their institutions' multi-generational missions.

While systemic changes may begin to show benefits within 5-10 years, the full realisation of addressing major systemic risks such as climate change or social inequality might unfold over 20-30 years or more.

This longer view allows faith-consistent investors to consider risks and opportunities that short-term focused investors might systemically overlook.

Two core beliefs underpin this argument:

1 **The importance of focusing on long-term success:** Nearly all faiths and faith-based organisations think in terms of generational impact and therefore aspire for their missions to endure over decades or even centuries, as seen in Sikhism's 300-year cycles. Successful investing requires a long-term perspective, yet the investment industry often fixates on short-term results.

This myopic focus can lead to irrational and suboptimal decisions that jeopardise the long-term sustainability of organisations. Valuing long-term perspectives means companies are more likely to weather temporary dips and crises in the market better than businesses focused on short-term gains. In other words, if a company plans long term, their values are already in part aligned with faiths who invest long term.

2 **The power of investing for positive impact:** While maintaining rigorous attention to traditional investment metrics, faith-consistent investors also identify opportunities in markets that are often overlooked, under-researched, or misperceived as being overly risky due to bias against investments with positive social impact.

These ‘inefficient markets’ exist not because the underlying investments are inherently less profitable, but because conventional investment approaches may overlook them due to misplaced assumptions about the relationship between impact and returns.

By recognising and investigating these market inefficiencies, faith-consistent investors can identify investments that deliver both strong financial returns and positive societal outcomes. The key insight is not that traditional financial metrics should be replaced, but that opportunities exist precisely because others have incorrectly assumed that social benefits and financial returns are mutually exclusive.

The sustainable economy framework: A faith-based approach
A sustainable economy balances three key pillars—social cohesion, long-term prosperity for all, and environmental health. This framework recognises that economic success is inextricably linked to the wellbeing of people and the planet.

For faith-consistent investors, this concept aligns closely with many religious teachings about stewardship, balance, justice, and care for creation. More importantly, it provides a roadmap for identifying investments that are positioned for long-term success.

Addressing systemic risks
One of the primary ways a sustainable economy approach to investing can enhance returns is through the mitigation of systemic risks: large-scale challenges that affect the entire economic system, such as climate change, social inequality, and poor governance practices. Traditional investment approaches often overlook these risks, focusing instead on company-specific factors.

However, systemic risks can have profound impacts on long-term investment performance. By addressing these risks, faith-consistent investors can potentially improve their returns while also advancing their values.

Examples of how FCI addresses systemic risks include:

1 **Environment and climate change:** Many faith traditions emphasise care for creation. This principle can guide investments in companies that are proactively addressing climate risks and developing clean technologies, potentially positioning portfolios for success in an economy transitioning to a low-carbon future.

For example, companies that invested early in renewable energy technologies have often seen their market valuations increase as global demand for clean energy solutions grows, both from consumers and institutional investors seeking to reduce their fossil fuel exposure.

2 **Social inequality:** The principle of justice, common across faiths, can lead to investments in companies that promote fair labour practices and community development.

This can mitigate risks associated with social unrest and promote more stable, prosperous communities—which in turn can support economic growth. Companies that emphasise fair treatment of workers often experience lower turnover rates, higher productivity, and better customer relations, all of which can translate to stronger financial performance.

3 **Governance issues:** Faith teachings on integrity and accountability align well with strong corporate governance practices. Investing in well-governed companies can reduce risks of fraud, corruption, and mismanagement while promoting human flourishing.

For instance, companies that have implemented strong ethical governance frameworks typically experience fewer scandals, regulatory penalties, and operational disruptions, leading to more stable long-term performance.

BEYOND SHORT-TERM PERFORMANCE

A broader view of investment success

One of the main limitations of current investment practices is an over-emphasis on idiosyncratic risks and short-term performance metrics, by which we mean those in the quarterly or the 1- to 3-year time frame. Collectively, the investment community has been almost exclusively focused on managing these short-term, company-specific risks, devoting virtually all of its energy and resources to beating performance benchmarks and ranking high in their peer universes.

But investing focused strictly on idiosyncratic risks is, by definition, a 'zero-sum minus' game. It's 'zero-sum' because one investor's outperformance must be matched by another's underperformance. It becomes 'minus' when we factor in the excessive fees paid to asset managers and the transaction costs incurred from frequent trading.

By contrast, systemic risk management focuses on issues that affect the entire market, which will ultimately improve overall market returns—producing a rising tide that lifts all boats. If all investors shift a portion of their governance attention to addressing systemic risks, all investors will realise better outcomes.

This is a difficult concept for many to accept because one cannot measure the extent to which such efforts to manage systemic risks were successful, unlike managing idiosyncratic risks, which can be measured with quarterly performance results.

Promoting systemic change will take time and will not result in improved results immediately, but rather gradually over time. What's more, the results from successfully addressing systemic change cannot be easily measured because there is no alternative universe with investment returns that reflect no systemic change. Yet despite these measurement challenges, failing to address systemic risks leads, in the long term, to poorer results for all market participants as these risks eventually materialise in the form of market disruptions, regulatory penalties, or stranded assets.

To summarise the points on the previous page: too often, asset owners allocate most of their governance 'budget' to maximising results based on near-term benchmarks. They compare their performance to indices and to other asset owners, often making sub-optimal decisions that seek to maximise near-term gains while ignoring systemic issues that may impair long-term results.

Faith-consistent investors, with their focus on long-term stewardship and values alignment, are well-positioned to avoid this short-term trap and contribute to a market environment where all participants can benefit. It is not just faith-consistent investors that will benefit, but all investors will ultimately benefit from achieving systemic and sustainable change—as mentioned earlier—'a rising tide that lifts all boats'.

Faith-driven wisdom for long-term risk stewardship

We've noted that across various faith traditions, we find common principles that align closely with sustainable economic practices. These include concepts of stewardship, balance, justice, human dignity, and care for creation. When applied to investing, these principles can guide investors towards practices that not only uphold their values but also mitigate long-term risks.

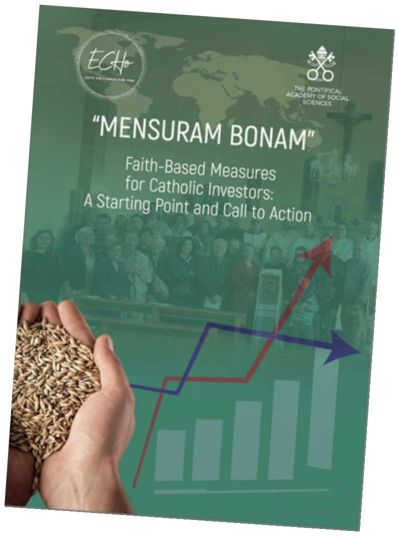
Faithful stewardship: Engaging versus excluding?

When confronted with companies that don't align with faith values, investors face a choice: exclude (or divest) or engage, i.e., the strategic choice investors face between removing certain companies from their portfolios due to harmful practices or remaining invested to influence those companies through the dialogue and advocacy of engagement.

Almost all faiths will exclude investments that conflict directly with their beliefs and teachings, and, indeed, this is often the starting point in the development of a faith-consistent investment policy. In other cases, however, the decisions may be more nuanced as perspectives and priorities change over time.

Yet, while exclusions/divestment may be appropriate in some cases, engagement can provide an opportunity to influence corporate behaviour positively. For example, the UK-based Church Investors Group (CIG) represents the charitable and pension funds of 67 denominations, dioceses, religious orders, and Christian-based charities, with combined investment assets of more than £26 billion.

It considers its annual recommendations for proxy voting for its membership to be 'one of our most important actions to influence business practice'. In recent years, CIG has engaged on topics as varied as climate change, modern slavery, living wage (the minimum income necessary for a worker to meet their needs), child labour, and tax transparency, demonstrating that faith-based investors can effectively advocate for positive change within the corporate world.



Likewise, *Mensuram Bonam*, published in 2022 by the Pontifical Academy of Social Sciences as a guide for Catholic investors, describes faith-consistent investing as comprising three calls to action in practice, of which the first is the call to engage (followed by calls to enhance and to exclude).

It says: 'The goal of the engagement process is for investors to actively leverage their ownership to influence—through dialogue, mutual learning, and collaboration—the enterprises in which they invest... Active engagement is therefore an indispensable element in any faith-consistent investment policy' (*Mensuram Bonam*, pg 30).

Effective engagement—whether conducted directly by the faith organisation or through their asset managers—allows faith investors to leverage their moral authority, long-term perspective, and financial influence to advocate for substantive reforms.

Faith-based investors should therefore make engagement a cornerstone of their investment strategy, insisting that their asset managers demonstrate robust engagement capabilities and providing clear guidance on priority issues that reflect their faith values. By doing so, they move beyond merely avoiding harm to actively shaping a more just and sustainable economic system aligned with their deepest beliefs, as we have written about previously in our research posts.

SERVING MISSION & MANDATE
Aligning faith and fiduciary duty

Some argue that considering faith values in investment decisions conflicts with fiduciary duty. However, as our understanding of risk evolves to include environmental, social, and governance factors, it's increasingly clear that FCI usually aligns closely with fiduciary responsibility.

By considering a broader range of risks and opportunities, faith-consistent investors can make more informed decisions that support long-term value creation. This approach is entirely compatible with the fiduciary obligation to act in the best interests of beneficiaries.

Addressing market failures: The economic rationale for faith-consistent investing
Interestingly, faith-consistent investing also aligns with traditional capitalist principles, offering a compelling economic rationale beyond its moral foundation.

As Mike Even, co-founder of FaithInvest, argues: 'While capitalism is brutally efficient in allocating resources and creating optimal economic outcomes, it does have recognised imperfections. These imperfections create opportunities where FCI can potentially enhance market function and portfolio performance.'

Two key market imperfections that FCI can address include:

1 **Externalities** occur when the economic activities of one entity affect others without this being reflected in market prices—these are the costs or benefits not accounted for in market transactions. Environmentally negative externalities, such as greenhouse gas emissions, provide a clear example—while some markets have introduced carbon pricing, in many cases these mechanisms are limited or insufficient, allowing profit-maximising entities to overlook the true social and environmental cost of greenhouse gas emissions.

When faith-consistent investors address such externalities through portfolio choices, they are engaging where traditional market systems fall short. This approach may also contribute to risk mitigation or long-term performance enhancement as regulatory frameworks and societal expectations continue to evolve.

2 **Agency theory** refers to the challenges that arise when one party (the agent), such as a corporate manager or investment professional, is tasked with acting on behalf of another (the principal), such as shareholders or asset owners. Agency issues emerge when the agent's incentives—often tied to short-term performance—diverge from the long-term interests of the principal. In the context of FCI, initiatives that prioritise worker well-being and life quality can help address these misalignments.

By promoting values such as dignity, fairness, and long-term stewardship, FCI approaches may not only reflect moral commitments but also reduce risk and enhance returns by fostering more stable, resilient organisations over time.

THE GOVERNMENT'S ROLE
in enabling faith-consistent investing

While emphasising the benefits of market-based approaches, it's important to recognise that government has a crucial role in addressing the existential challenges that unfettered capitalism can create—particularly those broad systemic issues that markets alone cannot solve.

Government regulation, when properly implemented, helps level the playing field for all economic actors. For instance, regulations protecting worker safety ensure that companies prioritising safety aren't disadvantaged compared to those cutting corners. Similarly, environmental regulations protect responsible companies from unfair competition by those that ignore environmental stewardship

Clear and credible regulation also plays an important role in shaping investor sentiment and expectations. Markets respond not just to prices, but to signals—regulatory clarity provides the long-term policy certainty investors need to allocate capital confidently. For systemic risks like climate change, strong regulatory frameworks can accelerate the flow of investment into climate friendly technologies and resilient infrastructure by reducing uncertainty and correcting market failures.

When governments set consistent rules—such as carbon pricing, climate disclosure standards, or clean energy incentives—they guide market behaviour, reduce risk premiums, and catalyse innovation. In this way, good regulation doesn't stifle markets; it strengthens them by aligning private incentives with the public good and ensuring that long-term sustainability is factored into financial decision-making.

The key lies in finding the right balance.
While addressing the burden of conflicting and duplicative regulations that discourage innovation, we shouldn't abandon the principle of thoughtful regulation altogether. Instead, we should focus on creating clear, consistent ‘rules of the road’ that ensure fair competition while promoting the goals of a sustainable economy.

For faith-consistent investors, this regulatory environment creates both opportunities and responsibilities.

As values-driven stakeholders with long-term horizons, faith-consistent investors can play an influential role in advocating for sensible regulatory frameworks that address systemic risks and promote market integrity. Through collaborative engagement with policymakers, faith-consistent investors can help shape regulations that align economic incentives with broader societal well-being—extending their impact beyond individual investment decisions.

Faith-based asset owners must recognise that their moral responsibility extends beyond portfolio construction to include active participation in shaping the systems that govern markets. Public policy is an important lever for addressing systemic risks at scale—no amount of individual investment decisions can match the impact of well-designed regulations that influence capital flows across entire economies.

Therefore, faith organisations serious about creating lasting change should commit to joining investor coalitions that engage with policymakers, adding their distinct moral voice to advocacy efforts promoting policies that address climate change, social inequality, and other systemic challenges.

This involvement is not peripheral to faith-consistent investing—it's essential to its success and represents a thoughtful opportunity to translate faith values into structural economic transformation.

The time for faith-based leadership is now

In times of uncertainty, leadership often emerges from unexpected places. As pressure mounts against sustainable and responsible investing practices—particularly in the United States—faith-based investors find themselves at a defining moment. This is a time not to step back, but to lead boldly, guided by both moral conviction and a long-term vision rooted in faith.

Faith organisations collectively hold hundreds of billions of dollars in assets and share fundamental values that transcend denominational boundaries: caring for the poor, pursuing justice, showing mercy, and practicing responsible care of our world. Unlike many institutional investors constrained by external pressures, faith-based organisations maintain the independence to align their investments with their values.

Every dollar aligned with faith values becomes a force for positive change. This combination of values, financial influence, and institutional independence positions faith organisations to lead in shaping a more just, sustainable, and values-driven economy. As more faith-based investors step forward into faith-consistent investing, they create a potent, transformative, demonstration effect, showing that it's possible—and profitable—to invest in alignment with values of justice, sustainability, and human dignity.

CONCLUSION

Faith-consistent investing (FCI) is not about sacrificing returns for values. Instead, it's an approach that uses faith principles as a guide for identifying and mitigating risks while capitalising on opportunities that arise from building a more sustainable and just economy.

By focusing on long-term value creation, addressing systemic risks, and engaging with companies to promote better practices, faith-consistent investors can potentially enhance their returns while staying true to their values. As we face increasing global challenges, our view is that this approach to investing will prove not just ethically sound, but financially prudent as well.

The concept of a sustainable economy provides a persuasive framework for FCI. By focusing on social cohesion, long-term prosperity, and environmental health, investors can address systemic risks, capitalise on emerging opportunities, and potentially enhance their long-term returns.

It's important to acknowledge that true FCI is a long journey. One often starts out with ethical exclusions, but the true transformative nature of FCI lies in engagement and investing for impact. As Dave Zellner concludes: ‘I strongly believe that the bulk of faith-consistent investment efforts should focus on engaging for change and investing for impact.’

This approach not only honours religious values but also contributes to building a more sustainable global economy that benefits both people and the planet.

As mentioned earlier in this paper, FaithInvest understands the challenges and concerns that faith-based organisations face when seeking to align their investments with their values. We recognise that this journey can seem complex, but we're here to support you every step of the way.

Is your faith organisation ready to take a first step—or a further step—toward FCI? FaithInvest can help, with free assessments of faiths' investment policies and guidelines, one-on-one projects, resources on faith-consistent investing, and training programmes. Reach out to us at info@faithinvest.org.

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