CERTIFICATE IN ESG INVESTING
V.1 TESTED FROM 2 September 2019

UNIT AIMS

By the end of this unit, learners should be able to demonstrate:

- An understanding of the context for different approaches to Responsible Investment and specifically, consideration of Environmental, Social and Governance (ESG) factors
- An understanding of the underlying issues that constitute factors within each of the Environmental, Social and Governance areas
- An understanding of the broader sustainability context and global initiatives
- An understanding of the ESG Market: relevance, size scope, key drivers and challenges and risks and opportunities
- An understanding of governance factors, key characteristics, main models and material impacts
- An understanding of environmental factors, systemic relationships, material impacts, mega trends and approaches to environmental analysis at country, sector, and company levels
- An understanding of social factors, systemic relationships, material impacts and approaches to social analysis at country, sector and company levels
- An understanding of ESG analysis, valuation and integration
- An ability to analyse how ESG factors may affect industry and company performance and affect company valuation
- An understanding of engagement and stewardship
- An understanding of ESG integrated portfolio construction and management
- An ability to apply ESG screens to the main asset classes and their sub-sectors
- An understanding of investment mandates, portfolio analytics and client reporting
Question allocation across the syllabus is balanced on the guidance of psychometric and industry specialists. The following question allocation for Version 1 of the Certificate in ESG Investing is provided as a broad indication of the relative 'weighting' of different parts of the syllabus in examinations from 2 September 2019.

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**OTHER INFORMATION REGARDING THIS UNIT:**

- **Exam format:** 100 questions
  Online testing using standard multiple choice and item set questions
- **Time allowed for exam:** 2 hours and 20 minutes
- **Grades:** Pass or Fail
- **Study Materials:** Official Training Manual v.1 is available from the CFA UK website; specimen exam available on CFA UK website.
- **Recommended study hours:** 130 hours
- **Availability of exam sessions:** Every working day through Pearson VUE testing centres.
TOPIC 1  INTRODUCTION TO ESG

1.1  INTRODUCTION TO ESG

1.1.1 Explain the different approaches to Responsible Investment

• Ethical / Values-driven Investment
• Social & Responsible Investment (SRI)
• Environmental, Social & Governance (ESG)
• Thematic Investment
• Impact Investment

1.1.2 Describe the benefits to organisations of adhering to good practice in ESG

1.1.3 Explain in outline the arguments for and against ESG / sustainable investment as a strategy, and in relation to financial system stability and effectiveness

1.1.4 Explain in outline the systemic nature of ESG issues in terms of key components / concerns and some of the risks, uncertainties and knock-on effects that they can pose:

• Environmental: climate change, infrastructure, natural resources, nuclear energy, sustainability
• Social: human capital, culture, customer engagement
• Governance: employee relations, management structure, executive remuneration
• Disclosure and regulation
• Technological disruption
• Demographical and social change
• Globalisation of value chains
• Changes to the distribution and transfer of wealth

1.1.5 Explain the framework of meta-geopolitics and power dynamics impacting on global governance, corporate structures and ESG issues:

• Domestic politics
• Economics
• Environment
• Health and social care
• Human and scientific resourcefulness
• Military and security
• International diplomacy
• Legal, accounting and financial standards
• Attitude to corruption and corporate fraud

1.1.6 Distinguish between the aims and elements of key supranational geo-political ESG initiatives, and the progress achieved to date:
• United Nations Global Compact (UNGC) Principles
• United Nations Sustainable Development Goals (SDGs)
• Principles for Responsible Investment (PRI)
• The Paris Agreement and United Nations Framework Convention on Climate Change (UNFCCC)
• Financial Stability Board Task Force in Climate-related Financial Disclosures (TCFD)

1.1.7 Define the following sustainability based concepts in terms of their strengths and shortcomings:

• Three corporate pillars of sustainability
• Triple bottom line (TBL) accounting

TOPIC 2 THE ESG MARKET

2.1 THE ESG MARKET

2.1.1 Explain the relevance, size and scope of ESG investing:

• In relation to the economy
• Within financial markets
• Distribution by asset class, investor type, geographical
• Stakeholder structure and relationships
• Market structure

2.1.2 Explain key market drivers in favour of ESG integration:

• Investor demand / intergenerational wealth transfer
• Regulation and “soft law”
• Public awareness
• Data sourcing and processing improvements

2.1.3 Explain the key drivers and challenges for ESG among stakeholders within the investment industry:

• Governments / public agencies
• Pension funds, investment consultants and trustees
• Investment and financial institutions
• Insurance Companies – a) as insurers and b) as investors
• Corporate and other major shareholders
• Private Wealth / Retail
• Regulators
• Professional member and trade organisations
• Sustainability / collaboration platforms
2.1.4 Explain how ESG-related issues can create both risks and opportunities for investors

2.1.5 Explain how ESG issues are related to sustainability trends and themes within the investment industry, including:
  - the longer-term nature of ESG investing
  - ESG-driven market, organisational and cultural changes

2.1.6 Explain the key challenges to the implementation of successful ESG investing:
  - Investment mandate interpretation and screening application
  - Isolating the impact of ESG
  - Strategy definition: risk management vs. value creation / materiality
  - Portfolio construction and management tools
  - Available expertise and specialism
  - Disclosure of internal standards and practices
  - Pace of change and development in ESG
  - Data quality, variability and interpretation
  - Identifying material ESG factors

2.1.7 Describe the growing body of academic and industry research correlating ESG performance to corporate performance and shareholder returns

TOPIC 3  GOVERNANCE FACTORS

3.1 GOVERNANCE FACTORS

3.1.1 Explain the evolution of corporate governance frameworks and key motivators for step change:
  - Development of corporate governance
  - Roles and responsibilities
  - Systems and processes
  - Performance metrics and KPIs
  - Shareholder engagement
  - Alignment with minority stakeholders

3.1.2 Assess key characteristics of effective corporate governance, and the main reasons why they may not be implemented or upheld:
  - Board structure and independence
• Board composition, quality and skills
• Executive remuneration
• Financial integrity and transparency
• Diversity
• Capital allocation

3.1.3 Assess and contrast the main models of corporate governance in major markets and the main variables influencing best practice:

• Markets: Germany, Japan, Netherlands, Scandinavia, UK and USA
• Extent of variation of best practice
• Differences in legislation, culture and interpretation

3.1.4 Explain the challenges encountered by Auditors in relation to promoting best practice in corporate governance and preventing corporate fraud:

• Conflicts of interest: audit / consulting / tax and other specialist services
• Reliance on internal audit
• Collusion: intentional and unintentional
• Technological disruption
• Legal accountability

3.1.5 Assess material impacts of governance issues on potential investment opportunities, including the dangers of overlooking them:

• Public Finance Initiatives
• Companies
• Infrastructure / private finance vehicles
• Societal impact

3.1.6 Apply material corporate governance factors to:

• Financial modelling
• Ratio analysis
• Risk assessment
• Quality of management
4.1 ENVIRONMENTAL FACTORS

4.1.1 Explain key environmental issues from an evidence-based perspective, including:

- Climate change
- Natural resources
- Pollution and waste
- Environmental opportunities: clean tech, renewable energy, green building

4.1.2 Explain the systemic relationships and activities between business activities and ecosystem services, including:

- Biodiversity issues
- Supply, operational and resource management issues
- Supply chain transparency and traceability
- Risk mitigation and management strategies

4.1.3 Assess material impacts of environmental issues on potential investment opportunities, including the dangers of overlooking them:

- Public Finance Initiatives
- Companies
- Infrastructure / private finance vehicles

4.1.4 Assess key “megatrends” influencing environmental change in terms of potential impact on companies and their environmental practices:

- Public perception of Value
- Authenticity and capacity to maintain ESG credentials
- Incentives and disincentives for “gaming the system”
- Managing the tension between consumer trends and long-term sustainability
- Regulation
- Consumer demand: sustainability vs. consumerism
- Political: trade tariffs / subsidies / collaboration vs competition
- Physical risks: flooding, drought, climate change

4.1.5 Identify approaches to environmental analysis at country, sector and company levels in both developed and emerging countries

4.1.6 Apply material environmental factors to:

- Financial modelling
TOPIC 5 SOCIAL FACTORS

5.1 SOCIAL FACTORS

5.1.1 Explain key social issues from an evidence-based perspective:

- Human Capital: development, employment standards, health and safety, product liability / consumer protection: safety, quality, health and demographic risks, data privacy and security
- Stakeholder opposition/ controversial sourcing
- Social opportunities: access to communications, finance, health and nutrition
- Social and news media
- Animal welfare

5.1.2 Explain the systemic relationships and activities between business activities and social issues, including:

- Inequality
- Globalisation
- Automation and AI in manufacturing and service sectors
- Wealth creation
- Work, family and leisure time
- City vs rural communities
- Health and welfare
- Supply chain

5.1.3 Assess material impacts of social issues on potential investment opportunities, including the dangers of overlooking them:

- Changing demographics, including health and longevity
- Digital disruption, social media and e-mobility
- Individual rights and responsibilities
- Family structures and roles
- Education and work
- Roles of religion and secularism within society
- Inequality
- Globalisation

5.1.4 Identify approaches to social analysis at country, sector and company levels in both developed and emerging economies
5.1.5 Apply material social factors to:

- Financial modelling
- Ratio analysis
- Risk assessment
- Quality of management

TOPIC 6 ESG ANALYSIS, VALUATION AND INTEGRATION

6.1 ESG ANALYSIS, VALUATION AND INTEGRATION

6.1.1 Explain the aims and objectives of integrating ESG into a firm’s investment process

6.1.2 Describe different approaches of integrating ESG analysis into a firm’s investment process

6.1.3 Describe the challenges of integrating ESG analysis into a firm’s investment process:

- Financial
- Operational
- Cultural

6.1.4 Explain how ESG complements traditional financial analysis

6.1.5 Analyse how ESG factors may affect industry and company performance

6.1.6 Analyse how ESG factors may affect company valuation

6.1.7 Describe quantitative approaches to ESG analysis

6.1.8 Describe qualitative approaches to ESG analysis

6.1.9 Describe primary and secondary sources of ESG data and information

6.1.10 Explain the range of ESG integration databases and software available, and the nature of the information provided:

- SASB material sustainability issues: sector and industry
- MSCI ESG Ratings Methodology
- Sustainalytics
6.1.11 Explain how Credit Rating Agencies (CRAs) approach ESG Credit Scoring, and the extent to which CRA ratings can be relied upon for ESG investing:

- PRI Statement on ESG in Credit Ratings
- Main ESG CRA methodologies
- Quantitative ESG Scores (QESGs)
- Relationship between Scores and Ratings, and other indicators eg CDS Spread
- Key challenges: transparency, consistency and comparability

6.1.12 Identify the main providers of screening services or tools, similarities and differences in their methodologies, and the aims, benefits and limitations of using them

6.1.13 Explain the main applications of sustainability data systems within the investment analysis process:

- “Big data” analysis of multiple ESG factors
- Resource / supply, operational and price risk mitigation
- Evidence to support and guide sustainability practices
- Resource- and operations-related
- Modelling future sustainability scenarios, including climate change, wage growth, social effects
- Shift from static to real-time dynamic analysis

6.1.14 Describe the limitations and constraints of information provided by ESG integration databases

6.1.15 Describe the challenge of identifying and assessing material ESG issues

6.1.16 Describe the role of the Sustainable Accounting Standards Board (SASB) and the SASB Materiality Map as it relates to sector analysis

6.1.17 Identify tangible and intangible material ESG-related factors through both qualitative and quantitative approaches

6.1.18 Describe the challenges of undertaking ESG analysis across different geographic regions and cultures

6.1.19 Assess ESG issues using risk mapping methodologies

6.1.20 Describe how scorecards may be developed and constructed to assess ESG factors

6.1.21 Interpret a company’s disclosure on selected ESG topics

6.1.22 Apply the range of approaches to ESG analysis and integration across a range of asset classes
7.1 ENGAGEMENT AND STEWARDSHIP

7.1.1 Explain the purpose of investor engagement and stewardship, and why it is considered beneficial

7.1.2 Explain how the collective responsibilities of an asset management firm can influence responsible practices within companies and industries

7.1.3 Explain how engagement is achieved in practice, including key differences in objectives, style and tone

7.1.4 Distinguish between different types of engagement depending on asset class, including:
   - Proxy voting
   - Collective engagement

7.1.5 Explain the main principles and requirements of Stewardship Codes as they apply to UK-based institutional asset management firms:
   - US ERISA Act guidelines
   - EU EFAMA Stewardship Code

7.1.6 Apply appropriate methods to establish an engagement approach:
   - Strategy and tactics: goal-setting
   - Identifying who to talk with
   - Formalities: hosting / agenda / managing expectations
   - Communication: approach / tone / managing tensions
   - Working towards agreement
   - Escalation techniques
   - ESG investment forums
8.1.1 Describe approaches for integrating ESG into the portfolio management process

8.1.2 Explain approaches for how internal and external ESG research and analysis is used by portfolio managers to make investment decisions

8.1.3 Explain how screening has evolved through different approaches to Responsible Investment, and the benefits and limitations of the main approaches

8.1.4 Identify the main indices and benchmarking approaches applicable to sustainable and ESG investing, noting potential limitations:

- MSCI ESG
- S&P ESG
- FTSE Russell and FTSE4Good
- Green Bond Indices
- ICE ESG indices
- GRESB

8.1.5 Apply ESG screens to the main asset classes and their sub-sectors:

- Fixed Income (government / sovereign / corporate / other)
- Equity (listed / private)
- Real Estate (infrastructure; commercial / residential property)

8.1.6 Explain how ESG screens can be embedded within investment mandates / portfolio guidelines to:

- Generate investment returns
- Manage portfolio risk

8.1.7 Distinguish between ESG screening of individual companies and collective investment funds:

- On an absolute basis
- Relative to sector / peer group data
8.1.8 Explain how the risk-return dynamic of portfolio optimisation is impacted by ESG-integrated investing

8.1.9 Evaluate different types of ESG/ SRI investment in terms of key objectives, investment considerations and risks:

- Full ESG integration
- Exclusionary screening
- Positive alignment/ Best in Class
- Active ownership
- Thematic investing
- Impact investing
- Other

8.1.10 Describe approaches to managing passive ESG portfolios

8.1.11 Explain the impact of ESG factors on Strategic Asset Allocation

TOPIC 9  INVESTMENT MANDATES, PORTFOLIO ANALYTICS AND CLIENT REPORTING

9.1 INVESTMENT MANDATES, PORTFOLIO ANALYTICS AND CLIENT REPORTING

9.1.1 Explain why mandate construction is of particular relevance and importance to the effective delivery of ESG investing

9.1.2 Explain the most common features of ESG / responsible investing that Pension Consultants, Fund Selectors, and other Intermediaries are seeking to identify through RFP and selection processes:

- Voting
- Engagement
- Examples of decision making
- Screening process

9.1.3 Assess the different drivers (institutional, retail, private) that influence the type of ESG investing strategy selected

9.1.4 Explain the key challenges in measuring and reporting ESG-related investment performance:
• Active, passive and Smart Beta approaches
• Performance attribution
• Sensitivity analysis
• Risk measurement
• Engagement activity / impact
• Integrated reporting and investment review