CFA Society United Kingdom

CERTIFICATE IN ESG INVESTING

V.2 TESTED FROM 1 September 2020

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 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 governance factors, key characteristics, main models and material impacts
- An understanding of engagement and stewardship
- An understanding of ESG analysis, valuation and integration
- An ability to analyse how ESG factors may affect industry and company performance and security valuation across a range of asset classes
- An understanding of ESG integrated portfolio construction and management
- An ability to apply a range of approaches to ESG analysis and integration across a range of asset classes
- 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 2 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 1 September 2020.

Topic	Topic Name	Question Allocation
1	Introduction to ESG	4-8
2	The ESG Market	4-8
3	Environmental Factors	6-12
4	Social Factors	6-12
5	Governance Factors	6-12
6	Engagement & Stewardship	6-10
7	ESG Analysis, Valuation & Integration	20-32
8	ESG Integrated Portfolio Construction & Management	8-14
9	Investment Mandates, Portfolio Analytics & Client Reporting	4-8

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 Edition 2 will be 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 Define ESG

1.1.2 Define the following sustainability-based concepts in terms of their strengths and limitations:

- Corporate Social Responsibility
- Triple bottom line (TBL) accounting

1.1.3 Define the different approaches to ESG investing, their characteristics and the role that ESG plays in each of them:

- Responsible Investment
- Socially Responsible Investment (SRI)
- Sustainable Investment
- Best-in-Class Investment
- Ethical / Values-driven Investment
- Thematic Investment
- Impact Investment
- Green Investment
- Social Investment
- Shareholder Engagement

1.1.4 Describe the benefits and challenges to organisations of adhering to good practice in ESG and the arguments in relation to financial system stability and effectiveness

1.1.5 Explain in outline the materiality of ESG issues in terms of their key characteristics, risks and impact that they can cause:

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

1.1.6 Explain the different ESG megatrends, their systemic nature and potential impact on companies and company practices

1.1.7 Explain the aims, elements and progress achieved by key supranational ESG initiatives and organisations:

- United Nations Global Compact (UNGC) Principles
- United Nations Environment Programme Finance Initiative (UNEP FI)
- Principles for Responsible Investment (PRI)
- The Paris Agreement and United Nations Framework Convention on Climate Change (UNFCCC)
- United Nations Sustainable Development Goals (SDGs)
- International Corporate Governance Network (ICGN)
- Global Sustainable Investment Alliance (GSIA)
- Financial Stability Board Task Force on Climate-related Financial Disclosures (TCFD)
- Global Impact Investing Network (GIIN)
- Corporate Reporting Dialogue (CRD)

TOPIC 2 THE ESG MARKET

2.1 THE ESG MARKET

2.1.1 Explain the size and scope of ESG investing:

- In relation to the economy
- Within financial markets
- By asset class, investor type, geography and approach
- In relation to stakeholders

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 integration among stakeholders within the investment industry:

- Governments and regulators
- Pension funds, investment consultants and trustees
- Investment and financial institutions
- Insurance companies
- Corporations
- Private wealth / retail clients
- ESG rating and proxy voting service providers

- Trade and non-profit organisations and academia

2.1.4 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

2.1.5 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 versus. 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

TOPIC 3 ENVIRONMENTAL FACTORS

3.1 ENVIRONMENTAL FACTORS

3.1.1 Explain key concepts relating to climate change from an evidence-based perspective, including:

- Climate change
- Climate change mitigation
- Climate change adaptation and resilience measures

3.1.2 Explain key concepts relating to other environmental issues from an evidence-based perspective, including:

- Pressures on natural resources
- Pollution and waste

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

- Climate change and other environmental issues
- Supply, operational and resource management issues
- Supply chain transparency and traceability
- Systemic impact of climate risks on the financial system

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

- Growth of environmental and climate policies
- International climate and environmental agreements and conventions
- International initiatives
- Oceans and the blue economy

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

- Corporate and project finance
- Public Finance Initiatives
- Asset management

3.1.6 Identify approaches to environmental analysis at country, sector and company levels in both developed and emerging countries, including Natural Capital

3.1.7 Apply material environmental factors to:

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

3.1.8 Explain how companies and the investment industry can benefit from opportunities relating to climate change and environmental issues:

- Circular economy
- Green products
- Clean and technological innovation

TOPIC 4 SOCIAL FACTORS

4.1 SOCIAL FACTORS

4.1.1 Explain key social concepts 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 and microbial resistance

4.1.2 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

4.1.3 Assess key ‘megatrends’ influencing social change in terms of potential impact on companies and their social practices:

- Climate change
- Transition Risk
- Water Scarcity
- Mass migration

4.1.4 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 access to electronic services
- Individual rights and responsibilities
- Family structures and roles
- Education and work
- Distinction between faith-based ESG investing and exercise of religion as a social factor
- Inequality
- Globalisation

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

4.1.6 Apply material social factors to:

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

TOPIC 5 GOVERNANCE FACTORS

5.1 GOVERNANCE FACTORS

5.1.1 Explain the evolution of corporate governance frameworks and key motivators for step change:

- Development of corporate governance
- Roles and responsibilities
- Systems and processes
- Shareholder engagement
- Minority shareholder alignment

5.1.2 Assess key characteristics of effective corporate governance, and the main reasons why they may not be implemented or upheld:

- Board structure, diversity, effectiveness and independence
- Executive remuneration, performance metrics and KPIs
- Reporting and transparency
- Financial integrity and capital allocation
- Business ethics

5.1.3 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

5.1.4 Explain the role of auditors in relation to corporate governance and the challenges in effective delivery of the audit:

- Independence of audit firms and conflicts of interest
- Auditor rotation
- Sampling of audit work and technological disruption
- Auditor reports
- Audit liability
- Internal audit

5.1.5 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

5.1.6 Apply material corporate governance factors to:

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

TOPIC 6 ENGAGEMENT AND STEWARDSHIP

6.1 ENGAGEMENT AND STEWARDSHIP

6.1.1 Explain the purpose of investor engagement and stewardship

6.1.2 Explain why engagement is considered beneficial and its relationship with fiduciary duty

6.1.3 Explain the main principles and requirements of Stewardship Codes as they apply to institutional asset management firms:

- UK Walker Review (2009) and Stewardship Code (2020)
- US ERISA Act guidelines
- EU EFAMA Stewardship Code

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

6.1.5 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, including collective engagement
- ESG investment forums
- Proxy voting

6.1.6 Distinguish between different types of engagement across a range of asset classes (alternatives; equities; fixed income)

TOPIC 7 ESG ANALYSIS, VALUATION AND INTEGRATION

7.1 ESG ANALYSIS, VALUATION AND INTEGRATION

7.1.1 Explain the aims and objectives of integrating ESG into a firm's investment process

7.1.2 Describe different approaches of integrating ESG analysis into a firm's investment process

7.1.3 Describe the challenges of integrating ESG analysis into a firm's investment process:

- Financial
- Operational
- Cultural

7.1.4 Explain how ESG complements traditional financial analysis

7.1.5 Analyse how ESG factors may affect industry and company performance

7.1.6 Analyse how ESG factors may affect security valuation across a range of asset classes: alternative investments; equities; fixed income

7.1.7 Describe quantitative approaches to ESG analysis across a range of asset classes: alternative investments; equities; fixed income

7.1.8 Describe qualitative approaches to ESG analysis across a range of asset classes: alternative investments; equities; fixed income

7.1.9 Describe primary and secondary sources of ESG data and information

7.1.10 Explain the approaches taken across a range of ESG integration databases and software available, and the nature of the information provided

7.1.11 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 credit default swap (CDS) Spread
- Key challenges: transparency, consistency and comparability

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

7.1.13 Describe other uses of ESG and sustainability system data

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

7.1.15 Describe the challenge of identifying and assessing material ESG issues

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

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

7.1.18 Assess ESG issues using risk mapping methodologies

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

7.1.20 Interpret a company's disclosure on selected ESG topics

7.1.21 Apply the range of approaches to ESG analysis and integration across a range of asset classes: alternative investments; equities; fixed income

TOPIC 8 ESG INTEGRATED PORTFOLIO CONSTRUCTION AND MANAGEMENT

8.1.1 ESG INTEGRATED PORTFOLIO CONSTRUCTION AND MANAGEMENT

8.1.1 Explain the impact of ESG factors on strategic asset allocation

8.1.2 Describe approaches for integrating ESG into the portfolio management process

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

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

8.1.5 Explain the main indices and benchmarking approaches applicable to sustainable and ESG investing, noting potential limitations

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

- Alternative investments
- Equities
- Fixed Income

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

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

- Linking sustainable investing to the mandate
- Defining the sustainable investment strategy

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

- Generate investment returns
- Manage portfolio risk

9.1.3 Explain the most common features of ESG investing that asset owners and intermediaries, including Pension Consultants and Fund Selectors are seeking to identify through RFP and selection processes:

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

9.1.4 Explain the different client types and their objectives which influence the type of ESG investing strategy selected

9.1.5 Explain the key mechanisms for reporting on and monitoring performance and mandate alignment with client objectives.

9.1.6 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