

CERTIFICATE IN ESG INVESTING V.3

TESTED FROM 1 OCTOBER 2021

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, megatrends 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:

Question allocation across the syllabus is balanced on the guidance of psychometric and industry specialists. The following question allocation for Version 3 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 October 2021.

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 and stewardship	6–10
7	ESG analysis, valuation and integration	20–32
8	ESG integrated portfolio construction and management	8–14
9	Investment mandates, portfolio analytics and 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 3 will be available on the CFA Institute website.
 - Mock exam on CFA Institute website.
- Recommended study hours:**
- 130 hours.
- Availability of exam appointments:**
- Every working day through Prometric testing centres and every day via ProProctor remote-proctored exams.

TOPIC 1

INTRODUCTION TO ESG

By the end of this topic, learners should have:

- ▶ 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.

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 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 to organisations of adhering to good practice in ESG, and the linkages between these practices and financial system stability:
 - reduce costs and increase efficiency;
 - reduce risk of fines;
 - avoid costs from repercussions of investee's externalities; and
 - improve ability to benefit from sustainability megatrends.
- 1.1.5 Describe the challenges to organisations of adhering to good practice in ESG including:
 - Investment mandate interpretation and screening application.
 - Isolating the impact of ESG.
 - Strategy definition: risk management versus value creation/materiality.
 - Portfolio construction and management tools.
 - Disclosure of internal standards and practices.
 - Data quality, variability and interpretation.
 - Identifying material ESG factors.
- 1.1.6 Explain the materiality of ESG issues in terms of their key characteristics, risks and impact that they can cause.
- 1.1.7 Explain different ESG megatrends, their systemic nature and potential impact on companies and company practices.
- 1.1.8 Explain how ESG investing is a strategy and a practice, and the three ways in which investors typically reflect ESG considerations.
- 1.1.9 Explain the aims, elements and progress achieved by key supranational ESG initiatives and organisations:
 - United Nations initiatives.
 - Reporting initiatives.
 - Other initiatives.

TOPIC 2

THE ESG MARKET

By the end of this topic, learners should have:

- ▶ An understanding of the ESG market: relevance, size, scope, key drivers and challenges, and risks and opportunities.

2.1 THE ESG MARKET

- 2.1.1 Explain the history of ESG investing in brief, including its roots and modern responsible investment.
- 2.1.2 Explain the size and scope of ESG investing in relation to:
 - Geography.
 - Strategy.
 - Investor type.
 - Asset class.
- 2.1.3 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.
- 2.1.4 Explain the key drivers and challenges for ESG integration among stakeholders within the investment industry:
 - Asset owners.
 - Asset managers.
 - Fund promoters.
 - Financial services.
 - Policy makers and regulators.
 - Investees.
 - Government, civil society and academia.
- 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.

TOPIC 3

ENVIRONMENTAL FACTORS

By the end of this topic, learners should have:

- ▶ An understanding of environmental factors, systemic relationships, material impacts, megatrends and approaches to environmental analysis at country, sector and company levels.

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, including depletion of natural resources, water, biodiversity loss, land use and marine resources.
 - Pollution, waste and a circular economy.
- 3.1.3 Explain the systemic relationships between business activities and environmental issues, including:
- Systemic impact of climate risks on the financial system: climate-related physical and transition risks.
 - The relationship between natural resources and business.
 - Supply, operational and resource management issues.
 - Supply chain transparency and traceability.
- 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, regional and country-level policy and initiatives.
 - Carbon pricing.
- 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 in both developed and emerging countries, including:
- Company, project, sector, country and market level analysis.
 - Environmental risks including carbon footprinting and other carbon metrics, natural capital approach and climate scenario analysis.
- 3.1.7 Apply material environmental factors to financial modelling, ratio analysis and risk assessment.
- 3.1.8 Explain how companies and the investment industry can benefit from opportunities relating to climate change and environmental issues:
- Circular economy.
 - Clean and technological innovation.
 - Green and ESG-related products.
 - Blue economy.

TOPIC 4

SOCIAL FACTORS

By the end of this topic, learners should have:

- ▶ An understanding of social factors, systemic relationships, material impacts and approaches to social analysis at country, sector and company levels.

4.1 SOCIAL FACTORS

- 4.1.1 Explain the systemic relationships and activities between business activities and social issues, including:
- Globalisation.
 - Automation and artificial intelligence (AI).
 - Inequality and wealth creation.
 - Digital disruption, social media and access to electronic devices.
 - Changes to work, leisure time and education.
 - Changes to individual rights and responsibilities, and family structures.
 - Changing demographics, including health and longevity.
 - Urbanisation.
 - Religion.
- 4.1.2 Assess key ‘megatrends’ influencing social change in terms of potential impact on companies and their social practices:
- Climate change.
 - Transition risk.
 - Water scarcity.
 - Pollution.
 - Mass migration.
 - Loss and/or degradation of natural resources and ecosystem services.
- 4.1.3 Explain key social concepts from an evidence-based perspective:
- Human capital:
 - development;
 - employment standards; and
 - health and safety.
 - Product liability/consumer protection:
 - safety;
 - quality;
 - health and demographic risks; and
 - data privacy and security.
 - Stakeholder opposition/controversial sourcing.
 - Social opportunities:
 - access to communications;
 - finance; and
 - health and nutrition.
 - Social and news media.
 - Animal welfare and microbial resistance.

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

TOPIC 5

GOVERNANCE FACTORS

By the end of this topic, learners should have:

- ▶ An understanding of governance factors, key characteristics, main models and material impacts.

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 key performance indicators (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:
- Major markets.
 - 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.
 - Auditor 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.
 - Risk assessment.
 - Quality of management.

TOPIC 6

ENGAGEMENT AND STEWARDSHIP

By the end of this topic, learners should have:

- ▶ An understanding of 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 some of the key criticisms of engagement.
- 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 Employee Retirement Income Security Act (ERISA) guidelines.
 - EU European Fund and Asset Management Association (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.

TOPIC 7

ESG ANALYSIS, VALUATION AND INTEGRATION

By the end of this topic, learners should have:

- ▶ 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 ability to apply a range of approaches to ESG analysis and integration across a range of asset classes.

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 qualitative approaches to ESG analysis across a range of asset classes.
- 7.1.4 Describe quantitative approaches to ESG analysis across a range of asset classes.
- 7.1.5 Identify tangible and intangible material ESG-related factors through both qualitative and quantitative approaches.
- 7.1.6 Describe how scorecards may be developed and constructed to assess ESG factors.
- 7.1.7 Assess ESG issues using risk mapping methodologies.
- 7.1.8 Explain how ESG complements traditional financial analysis.
- 7.1.9 Analyse how ESG factors may affect industry and company performance.
- 7.1.10 Analyse how ESG factors may affect security valuation across a range of asset classes.
- 7.1.11 Interpret a company's disclosure on selected ESG topics.
- 7.1.12 Apply the range of approaches to ESG analysis and integration across a range of asset classes.
- 7.1.13 Describe the challenges of undertaking ESG analysis across different geographic regions and cultures.
- 7.1.14 Describe the challenges of identifying and assessing material ESG issues.
- 7.1.15 Describe the challenges of integrating ESG analysis into a firm's investment process.
- 7.1.16 Explain the approaches taken across a range of ESG integration databases and software available, and the nature of the information provided.
- 7.1.17 Identify the main providers of screening services or tools, similarities and differences in their methodologies, and the aims, benefits and limitations of using them.
- 7.1.18 Describe the limitations and constraints of information provided by ESG integration databases.
- 7.1.19 Describe primary and secondary sources of ESG data and information.
- 7.1.20 Describe other uses of ESG and sustainability systems data.
- 7.1.21 Explain how credit rating agencies (CRAs) approach ESG credit scoring.

TOPIC 8

ESG INTEGRATED PORTFOLIO CONSTRUCTION AND MANAGEMENT

By the end of this topic, learners should have:

- ▶ An understanding of ESG integrated portfolio construction and management.
- ▶ An ability to apply ESG screens to the main asset classes and their sub-sectors.

8.1 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

By the end of this topic, learners should have:

- ▶ An understanding of 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 request for proposal (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.