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Chapter 1
Introduction to ESG

CFA Certificate in ESG Investing

Agenda

Chapter 1: Introduction to ESG

1. What is responsible investment?
2. Types of responsible investment.
3. Why integrate ESG?
4. Putting ESG into practice.
5. Key initiatives.

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Introduction to ESG

What is responsible investment?

Sample Exam Question 1

Which of the following does not represent an example of a social factor?

A. Modern slavery.

B. Working conditions.

C. Pollution and resources.

D. Labour rights.

What is Responsible Investment?

ESG investing represents an approach to managing assets where investors explicitly acknowledge the relevance of the following factors in their investment decisions:

- **Environmental**
  - Factors that relate to the natural world
  - Examples: climate change, pollution, deforestation
- **Social**
  - Factors that affect the lives of humans where categories include management of human resources, local communities and clients
  - Examples: human rights, modern slavery, child labour
- **Governance**
  - Factors that involve issues inherent to the business model or common practice in an industry
  - It also considers the interest of wider stakeholder groups
  - Examples: bribery and corruption, executive pay, board diversity and structure

Investors will also consider their own role as owners and creditors, with the long-term return of an investment portfolio in mind.

Definition and Scope of ESG

There is no standard across the industry on breaking down environmental, social and governance issues. Examples of the definition and scope of ESG issue can be shown from two widely-referenced organisations:

ENVIRONMENTAL

- Climate change
- Resource depletion
- Waste
- Pollution
- Deforestation

SOCIAL

- Human rights
- Modern slavery
- Child labour
- Working conditions
- Employee relations

GOVERNANCE

- Bribery and corruption
- Executive pay
- Board diversity and structure
- Political lobbying and donations
- Tax strategy

Source: PRI.[1]

Source: FTSE Russell.[2]

Corporate Social Responsibility

Corporate social responsibility (CSR) is a wide business concept that describes a company's commitment to conducting business in an ethical way.

This has led to the concept of **triple-bottom line accounting** which expands the traditional accounting framework that is focused on profit to include two other performance areas: social and environmental impacts of the company.

These three bottom lines are often referred to as the **three P's**:

- **P**eople
- **P**lanet
- **P**rofit

In practice, they have been replaced in industry with a broader framework of sustainability that's is not just limited to accounting

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Introduction to ESG

Types of responsible investment

Sample Exam Question 2

Which of the following is not a form of ESG investment?

A. Sustainable Investment.

B. Green Investment.

C. Thematic Investment.

D. Value investment.

A Spectrum of Capital

	Philanthropy		Social impact investing		Sustainable and responsible investing	Conventional financial investing
	Traditional philanthropy	Venture philanthropy	Social invesing	Impact investment	ESG investing	Fully commercial investment
Focus	Address societal challenges through the provisions of grants	Address societal challenges with venture investment approaches	Investment with focus on social and/or environmental outcomes and some expected financial return	Investment with an intent to have a measurable environmental and/or social return	Enhance long-term value by using ESG factors to mitigate risks and identify growth opportunities	Limited or no regard for ESG practices
			Use of ESG metrics and methodologies			
Return expectation	Social return only	Social return focused	Social return and sub-market financial return	Social return and adequate financial market rate	Financial market return focused on long-term value	Financial market return only

Investment Types

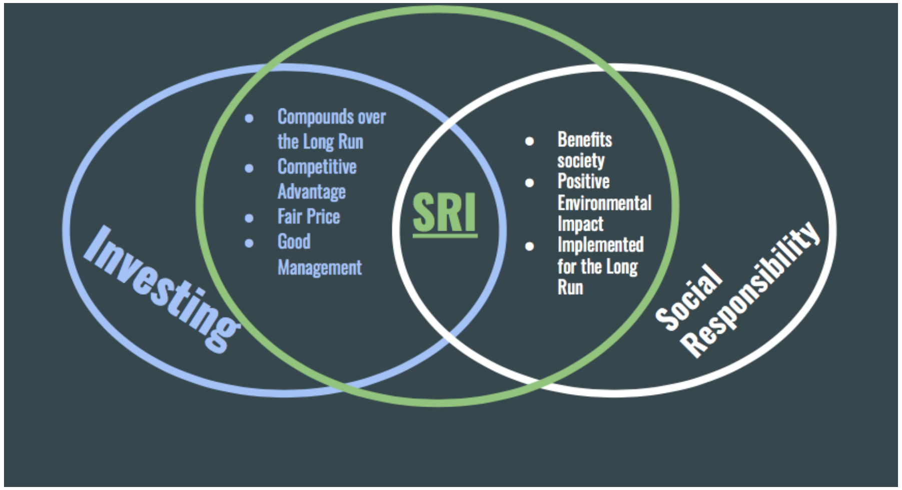
Responsible Investment

- Represents a strategy and practice that incorporates ESG factors into investment decisions and active ownership.
- It will consider how ESG might influence:
  - The risk-adjusted return of an asset and stability of an economy, and
  - How investment in, and engagement with, assets and investees can impact society and environment

Investment Types

Socially Responsible Investment (SRI)

- An approach that applies social and environmental criteria when evaluating companies.
- SRI investors generally score companies using a chosen set of criteria, using sector specific weightings. A hurdle is then set for inclusion within the investment universe. This serves as a first screen to identify a list of ESG qualified companies.
- SRI can be used in combination with:
  - Best-in-class investment
  - Thematic funds
  - High-conviction funds
  - Quantitative investment strategies



Source: Compounding Snowballs Blog

Investment Types

Best-in-class Investment

- Involves choosing only the companies that overcome a defined ranking hurdle.
- The ranking hurdle is created using ESG criteria within each sector or industry, where the factors are weighted according to the sector.
- The portfolio can then be created from the list of qualified companies
- Due to the all-sector approach, it is commonly used in investment strategies that attempt to maintain certain characteristics of an index e.g. regional or sectoral diversification, whilst also targeting companies with a higher ESG rating e.g. MSCI World SRI

Source: Ossiam

Investment Types

Sustainable Investment

- Selection of assets that contributes to a sustainable economy e.g. an asset that mitigates natural and social resource depletion
- May include best-in-class and also that of ESG integration, which considers how ESG issue impact an assets risk and return profile.
- Can be used to describe companies with positive impact or companies that will benefit from sustainable macro-trends.
- Can also be used to screen out activities considered contrary to long-term environmental and social sustainability e.g. oil exploration in Arctic regions.

Source: CFA Society, Boston

Investment Types

Thematic Investment

- Selection of companies that sit under a sustainability-related theme e.g. clean-tech, sustainable agriculture
- Thematic funds will choose companies within various sectors that are relevant to a theme
- Note, not all thematic funds are considered ‘responsible investments’. This will depend on the theme of the fund, and also the ESG characteristics of the investee companies.

Source: Journal of Portfolio Management

Investment Types

Green Investment

- Investment into assets that mitigate:
  - Climate change
  - Resource inefficiency
  - Biodiversity loss
  - Other environmental challenges
- Some examples include; pollution control, recycling, process innovation and energy efficiency.
- Can be considered a broad sub-category of thematic investing and/or impact investing.
- Green bonds are commonly used in this strategy where proceeds of the bond issue are used to raise money for environmental projects (*more detail in can be found in Chapter 3)*

Investment Types

Social Investment

- Investing into assets that address social challenges.
- Could be products that address the bottom of the pyramid (BOP), which represents the poorest two-thirds of the economic human pyramid.
- BOP has a market-based model to alleviate poverty whilst providing growth and profits for businesses that serve these communities. Examples include:
  - Micro-finance and micro-insurance
  - Access to basic telecommunication
  - Access to improved nutrition and healthcare
  - Access to (clean) energy
- Social impact bonds represent a mechanism to contract with the public sector which pays for enhanced social outcomes and passes on part of the savings achieved to the investors.

Investment Types

Impact Investment

- Investing into assets with the specific intent of generating positive, measurable social and environmental impact in conjunction with a financial return (which differentiates it from philanthropy).
- Usually associated with direct investments, such private equity, private debt and real estate.
- Provides capital to address the world’s most pressing challenges by investing in projects and companies that:
  - Offer access to basic services such as housing, healthcare and education
  - Promote availability to low-carbon energy
  - Support minority-owned businesses
  - Conserve natural resources

Source: CNote

- Impact investors have diverse financial return expectations.

Investment Types

Ethical (Value-driven) and Faith-based Investment

- Investing in line with certain principles, usually using negative screening:
  - Catholic investors seeking to avoid investing into companies that are involved in the production and sales of weapons
  - Shariah investors looking to follow Islamic religious principles e.g. seeking to avoid investments that pay interest
- The process typically avoids investing into companies whose products and services are deemed morally objectionable by the investor or certain religions, international declarations, conventions and voluntary agreements:
- Typical exclusions include tobacco, alcohol, pornography, weapons, nuclear power and breach of agreements e.g. Universal Declaration of Human Rights
- Faith-based investors have a history of shareholder activism to improve the conduct of the investee companies

Investment Types

Shareholder Engagement

- Active ownership by investors whereby the investor seeks to influence a corporation's decisions on matters of ESG
- Could be via dialogue with the corporate officers or through voting powers
- Complementary to the previously mentioned approaches to responsible investment
- Its effectiveness will usually depend upon the:
  - Scale of ownership as an individual or collective (concert party);
  - Quality of the engagement dialogue and method used; and
  - Whether divestment is identified as a possible sanction.

(Further detail on engagement will be covered in Chapter 6)

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Introduction to ESG

Why integrate ESG?

Sample Exam Question 3

A report by McKinsey and Company (2017) identified that while, until recently, 97% of the Fortune Global 500 were headquartered in developed economies, nearly half of the world's large companies are expected to be headquartered in emerging markets by 2025. Which megatrend does this relate to?

A. Emerging and urban.

B. Technological disruption.

C. Demographic changes and wealth inequality.

D. Climate change and resource scarcity.

Why Integrate ESG?

1. **Financial Materiality**
    A. Reduced cost and increased efficiency
    B. Reduced risk of fines
    C. Reduced externalities
    D. Improved adaptability to sustainability megatrends
2. **Financial Performance**
3. **Fiduciary Duty**
4. **Economics**
5. **Impact and Ethics**
6. **Client Demand**
7. **Regulation**

We will now go on to look at these in greater detail…

Financial Materiality

A. Efficiency and Productivity

- Sustainable business practices build efficiencies by conserving resources, reducing costs and enhancing productivity.
- A solid ESG proposition can help companies attract and retain quality employees, this enhances employee motivation and overall productivity.
- Research has identified that employee satisfaction is positively correlated with shareholder returns.

B. Reduced Risk of Fines and State Intervention

- State and federal government agencies are enacting regulations to protect the environment.
- Integrating sustainability into a company will position it to meet changing regulations in a timely manner.

Financial Materiality

C. Reduced Negative Externalities

- **Externalities** relates to situations where the production or consumption of goods and services creates costs (negative externality) or benefits (positive externality) to others that are not reflected in the prices charged for those goods or services.

- With **negative externalities**:

Private costs $<$ Societal costs

Creates market outcomes that are inefficient
and essentially leads to ‘Market Failures’

- Externalities are the main reasons governments intervene e.g. by taxing polluters an amount equal to the cost of the harm incurred by others.

- As environmental and social regulation and taxation rise, it is expected that an increasing proportion of this cost might be recorded within companies’ accounts (a process called internalisation).

Financial Materiality

C. Reduced Negative Externalities – continued.

- Internalisation can happen in many different ways, for example in the transportation industry:
  - **Market-based instruments** e.g. charges, taxes and tradable permits
  - **Regulatory instruments** e.g. vehicle emission and safety standards, traffic restrictions
  - **Voluntary instruments** e.g. agreements with the car industry to reduce CO_2 emissions from new passenger cars
- The internalisation of these externalities could significantly impact the costs and profits of companies' products and services, affecting their bottom line, and subsequently valuation.
- Also, the uncertainty surrounding the timing and extent of internalisation is a key component of the overall risk landscape facing investors.

Financial Materiality

D. Sustainability Megatrends

- Key players such as business leaders, investors, economists and governments are increasingly recognising the economic implications of:
  - Social challenges
  - Environmental issues
- Whereby these factors have interacted with:
  - The aftermath of the financial crisis
  - Ageing populations
  - The rise of emerging countries
  - Rapid advancement in technology
- This interaction increases the complexity and impact that environmental and social challenges have on sectors and businesses.
- Some widely identified megatrends are highlighted on the next slide.

Financial Materiality

D. Sustainability Megatrends – continued

- Four widely recognized megatrends include:
  - **Emerging markets and urbanisation**
    - While, until recently, 97% of the Fortune Global 500 were headquartered in developed economies, nearly half of the world's large companies are expected to be headquartered in emerging markets by 2025
    - Nearly half of global gross domestic product (GDP) growth between 2010 and 2025 will come from 440 cities in emerging markets – 95% of them small- and medium-size cities
    - This will impact the supply chain, workforce, expectation of the local community as well as where new consumers come from
  - **Technological innovation**
    - Accelerated adoption of technology attracts accelerated innovation
    - Unemployment created as robots replace humans
  - **Demographic changes and wealth inequality**
    - A rising and ageing population is straining a shrinking workforce which could hinder economic growth
  - **Climate change and resource scarcity**

Financial Materiality

D. Sustainability Megatrends – continued

- The risks that these megatrends pose on companies will give a better understanding their potential future success or failure.
- However, one of the key challenges of incorporating ESG in the investment process lies with **time horizons:**
  - It is difficult to predict the **value** of future losses (or gains)
  - It is difficult to **forecast** when the losses (or gains) might occur
  - Fund managers' performance is commonly assessed using shorter time horizons, as opposed to the longer ones over which ESG factors might have a material impact.
- Identifying the issues which are genuinely material to a sector and company is one of the most active challenges within ESG investment.

Challenges to Integrating ESG

- Challenges to taking a more proactive approach to ESG investing is present across the entire investment decision process.
  - Before wanting to implement ESG
    - The view that implementing ESG will have a negative impact on performance
    - The view that fiduciary duty prevents integrating ESG
    - Advice given by consultants and advisers, at times, has not been supportive of product that integrate ESG
  - Once the decision to implement ESG has been made
    - The lack of understanding of how to create a mandate that effectively promotes ESG
    - The view that it will take significant resources are required
    - The gap between marketing, commitment and delivery of funds regarding the ESG performance
- Some institutional investors feel that ‘Tilting’ the portfolio towards desired ESG characteristics conflicts with their obligation to invest prudently.
  - Straying from established market benchmarks will lead to increased tracking error.

Challenges to Integrating ESG

- Many investors are unsure of how to integrate ESG within request for proposals or mandates.
- Some investor-led initiatives hope to address the issue.
  - The International Corporate Governance Network (IGCN) have created the Model Mandate Initiative.
  - The University of Cambridge Institute for Sustainability Leadership have created a toolkit for creating long-term sustainable mandates.
  - The PRI has published many guidance documents to support asset owners.

Challenges to Integrating ESG

- The challenge of resource is a big factor for asset owners with funding constraints.
- Even when resource is available issues arise when trying to incorporate into typical financial models.
  - Data availability
    - Disclosure is still a significant challenge
    - Also limited by investors' understanding of the data and what is deemed material
  - Modelling
    - ESG factors are mostly long-term financial impacts making it hard to factor into models
    - Quantifying the impact of ESG factors is also a challenge
  - Valuation techniques
    - How to adjust the discount rate in a model in order to consider ESG risks
- As a result, ESG analysis is often qualitative in nature and used alongside traditional quantitative models.

Challenges to Integrating ESG

- ‘Greenwashing’ is a growing challenge to the industry.
- Greenwashing originally described misleading claims about environmental practices, performance or product.
- In recent times, it has been used more widely to incorporate ESG factors more broadly.
- Recently, the EU has created various initiatives to standardise claims around the green and ESG credential of funds and indices, which will contribute to a clampdown on greenwashing.

Financial Performance

- Growing recognition in the financial industry an academia that ESG factors influence financial performance.
- Also, engaging with companies on ESG issues can create value for both investors and companies.
- Evidence suggests that sustainable companies deliver higher positive financial performance.
- However, this correlation does not hold for fund performance, suggesting the inability to translate ESG analysis in alpha.

Fiduciary Duty

- Financial institutions or individuals, known as **fiduciaries**, manage money or other assets on behalf of beneficiaries and investors.
- Fiduciary duties exist to ensure that those who manage other people’s money act in their beneficiaries' interests, rather than serving their own.
- Historically, investors have used the concept of fiduciary duty as a reason not to incorporate ESG issues. This is due to the misconception that ESG factors are not financially material.
- More recent reports such as the *Freshfields Report* (commissioned by the United Nations Environment Programme Finance Initiative (UNEP FI)) have concluded:

“Integrating ESG considerations into an investment analysis so as to more reliably predict financial performance is clearly permissible and is arguably required in all jurisdictions.”

(Further detail on fiduciary duty is covered in Chapter 2)

Economics

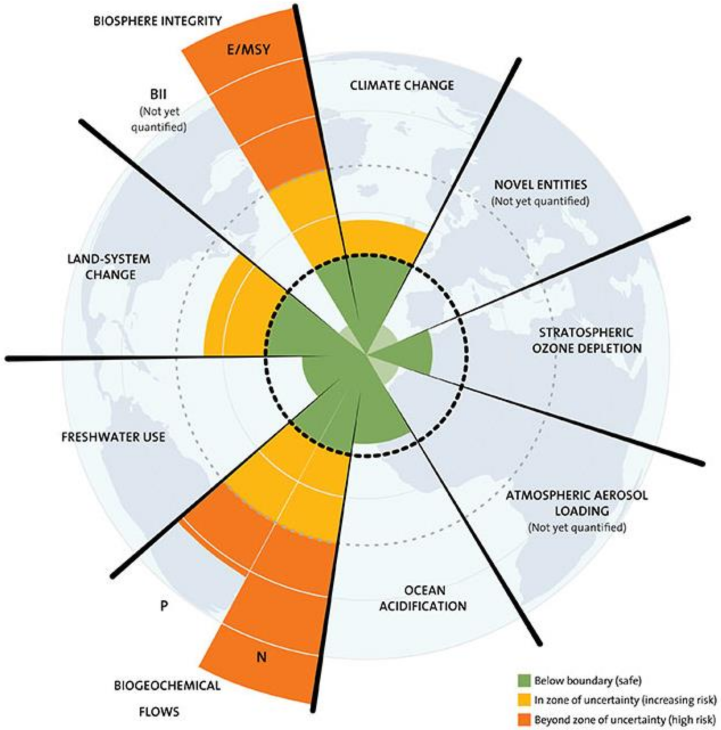
- Implementing ESG arises from the recognition that negative megatrends will, over time, create a pull on economic prosperity as inputs become more scarce and expensive.
- Also, the prevalence of health and income inequality increases instability geographically within countries and around the world.
- The Financial Stability Board (FSB) is an international body that monitors and makes recommendations about the global financial system.
- The FSB has identified climate change as a potential systemic risk

Economics

The Stockholm Resilience Centre identified 9 planetary boundaries. If we cross these boundaries, we threaten our ability to thrive and develop.

In 2015, the SRC assessment concluded that 5 of these boundaries had been crossed.

Climate change and biosphere integrity are ‘core boundaries’ which if crossed would ‘drive the Earth System into a new state’



Impact and Ethics

- Another reason for responsible investing comes from a belief by some investors that their investment can, or even should, serve society alongside providing a financial return.
- This translates into choosing investments with a positive impact and/or ignoring those with a negative impact

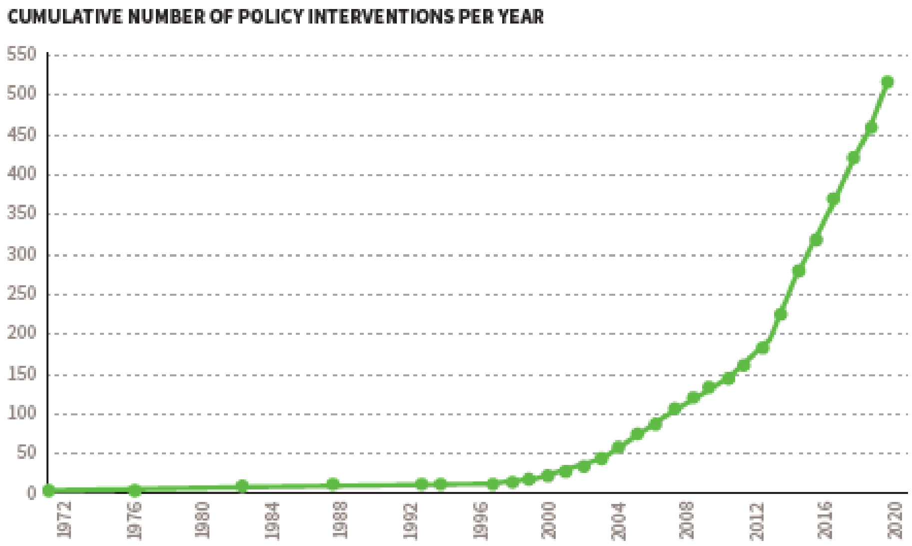
Client Demand

- Clients and pension fund beneficiaries are increasingly calling for greater transparency on how their money gets invested due to several factors:
  - Growing awareness of that ESG factors influence company value, returns and reputation
  - Increasing focus on the environmental and social impacts of the companies that they are invested into

(Further detail on demand and supply of RI is covered in Chapter 2)

Regulation

- Irrespective of investors views or beliefs, some investors are being required to increasingly consider ESG matters.
- A particular surge in policy intervention since the 2008 credit crisis.
- Regulatory change has also been driven by the realisation that financial sector can play a key role in meeting global challenges such as climate change



Source: PRI.[47]

(Further detail on impact of regulation on demand for RI is covered in Chapter 2)

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Putting ESG into practice

Sample Exam Question 4

Which one of the following is not typically a way that institutional investors typically reflect ESG considerations?

A. Investment decision-making.

B. Shareholder engagement.

C. Policy engagement.

D. Externality engagement.

United Nations Initiatives

Institutional investors typically reflect ESG considerations in three ways:

1. Incorporating ESG factors into **investment decision-making**
2. Through **corporate engagement**; and
3. Through **policy engagement**.

- Investment Decisions
  - ESG factors can be incorporated into investment decision-making throughout the investment value chain:
    - Asset owners requesting ESG factors in their **request for proposal** and integrating them into investment mandates and in the monitoring process
    - Asset owners and some asset managers can embed ESG into **strategic asset allocation (SAA)**
    - Asset managers and asset owners who invest directly can incorporate ESG issues within their **security selection process**

(Further detail on this process is covered in Chapters 7 and 8)

Putting ESG into Practice

- Shareholder Engagement
  - Investors can encourage investees to improve their ESG practice.
  - This could happen via a company meeting through voting powers or direct with the company's board or management team.
- Policy Engagement
  - Policy engagement by institutional investors is a natural extension of an investor's responsibility and fiduciary duty to act in the best interests of its beneficiaries.
  - Investors can work alongside regulators, standard setters and other parties (e.g. consultants, stock exchanges, etc.) to create a financial system that:
    - Sound and stable
    - Creates a level playing field
    - Brings ESG more effectively into financial decision-making
  - This can be achieved if investors respond to policy consultations, participate in initiatives and make recommendations to policy makers.

(Further detail on the above processes is covered in Chapter 6)

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Introduction to ESG

Key Initiatives

Sample Exam Question 5

Which one of the following is not one of the requirements implemented by the Principles of Responsible Investment (PRI) in 2018?

A. Investment policy that covers the firm’s responsible investment (RI) approach, covering >50% of assets under management (AUM).

B. Internal or external staff being responsible for implementing RI policy.

C. Senior-level commitment and accountability mechanisms for RI implementation.

D. Facilitate knowledge exchange

United Nations Initiatives

- The United Nations (UN) has played a critical role in the advancement of sustainability and specifically responsible investment in the past 30 years.
- Three of its initiatives are of particular interest to investors:
  - **United Nations Global Compact (UNGC)**
  - **United Nations Environment Programme Finance Initiative (UNEP FI)**
  - **United Nations Framework Convention on Climate Change (UNFCCC)**

United Nations Global Compact (UNGC)

- Launched in 2000 as a collaboration between leading companies and the UN
- Claims to be the largest corporate sustainability initiative in the world
- Over 8,000 corporate signatories spanning the globe
- Agree to adhere to 10 principles derived from broader global standards such as:
  - **Universal Declaration of Human Rights**
  - **International Labour Organization's Declaration on Fundamental Principles and Rights at Work**.
- Provides investors with a useful set of principles to assess and engage with companies, as well as directly aided companies in becoming more sustainable.

United Nations Environment Programme Finance Initiative (UNEP FI)

- Partnership between UNEP and the global financial sector to mobilise private sector finance for sustainable development.
- Started in 1992 and today works with 300 members – banks, insurers and investors.
- Established UNEP FI frameworks include:
  - **Principles for Responsible Investment (PRI)**, established in 2006 by UNEP FI and the UN Global Compact, now applied by half the world's institutional investors (US$83tn).
  - **Principles for Sustainable Insurance (PSI)**, established in 2012 by UNEP FI and today applied by one-quarter of the world's insurers (25% of world premium).
  - **Principles for Responsible Banking (PRB)** launched with more than 130 banks collectively holding USD47tn (GBP37tn) in assets, or one-third of the global banking sector, on 22 September 2019.

United Nations Environment Programme Finance Initiative (UNEP FI)

Principles for Responsible Investment (PRI)

- Comprises an international network of investors – signatories,
- A common goal to understand the implications of ESG to investment and ownership decisions and ownership practices
- The PRI provide support in four main areas:
  1. Broad range of tools and reports on best practice
  2. Hosts a collaborative engagement platform
  3. Reviews, analyses and responds to responsible investment-related policies and consultations
  4. The PRI Academy develops, aggregates and disseminates academic studies on responsible investment-related themes

United Nations Environment Programme Finance Initiative (UNEP FI)

The six voluntary PRI Principles

We will:

1. Incorporate ESG issues into investment analysis and decision-making processes.
2. Be active owners and incorporate ESG issues into our ownership policies and practices.
3. Seek appropriate disclosure on ESG issues by the entities in which we invest.
4. Promote acceptance and implementation of the principles within the investment industry.
5. Work together to enhance our effectiveness in implementing the principles.
6. Report on our activities and progress towards implementing the principles.

United Nations Environment Programme Finance Initiative (UNEP FI)

Reporting on Responsible Investment Practices

- The PRI does require members to report annually on their responsible investment practices, which are assessed by the PRI.
- The report is made available to the public.
- However, the assessment is private to the member, who can then decide whether, and with whom, they may wish to share it (e.g. asset managers share the report with an existing or prospective client asset owner).
- In 2018, the PRI implemented three minimum requirements:
  1. Investment policy that covers the firm’s responsible investment (RI) approach, covering >50% of assets under management (AUM).
  2. Internal or external staff being responsible for implementing RI policy.
  3. Senior-level commitment and accountability mechanisms for RI implementation.

United Nations Framework Convention on Climate Change (UNFCCC)

- Launched at the Rio de Janeiro Earth Summit in 1992, aims to stabilise greenhouse gas (GHG) emissions to limit man-made climate change.
- UNFCCC hosts annual Conferences of the Parties (COP) meetings, which seek to advance members states' voluntary agreements on limiting climate change:
  - COP3 meeting in Kyoto in 1997, which created the **Kyoto Protocol:**
    - Commits industrialised countries to limit and reduce their GHG emissions in accordance with agreed individual targets.
  - COP21 meeting in Paris in 2015, which led to the **Paris Agreement**:
    - Commits developed and emerging economies to strengthen the response to the threat of climate change by keeping a global temperature rise this century well below 2°C (3.6°F) above pre-industrial levels.

UN Sustainable Development Goals (SDGs)

- The **Sustainable Development Goals (SDGs)**, represents the UN's blueprint to address the key global challenges, including those related to poverty, inequality, climate change, environmental degradation, peace and justice.
- Agreed by all UN members in 2015
- The 17 goals are all interconnected and particularly aimed at governments.

Note from UN: The content of this publication has not been approved by the United Nations and does not reflect the views of the United Nations or its officials or Member States.

Source: Sustainable Development Goals.[50]

Other Initiatives

International Corporate Governance Network (ICGN)

- Investor-led organisation established in 1995 to promote effective standards of corporate governance and investor stewardship to advance efficient markets.
- The ICGN developed two key guidance documents for investors: one on stewardship and another one on investment mandates.

Global Sustainable Investment Alliance (GSIA)

- An international collaboration of membership-based sustainable investment organisations. It is a forum itself for advancing ESG investing across all regions and asset classes.
- Core members of the GSIA includes representatives from the regional responsible investment forums of Europe, the USA, Canada, Japan, Australia and New Zealand.

Other Initiatives

Task Force on Climate-related Financial disclosures (TCFD)

- The TCFD takes the Paris Agreement's 2°C (3.6°F) target and tries to operationalise it for the business world.
- From a climate-related risk perspective, it urges companies to disclose against the following:
  - **Governance**: the organisation's governance around climate-related risks and opportunities
  - **Strategy**: the actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy and financial planning
  - **Risk management**: the processes used by the organisation to identify, assess and manage climate-related risks
  - **Metrics and targets**: the metrics and targets used to assess and manage relevant climate-related risks and opportunities

(Further detail can be found in Chapter 3)

Other Initiatives

Global Impact Investing Network (GIIN)

- The GIIN focuses on lowering the barriers to impact investment by building critical infrastructure and developing activities, education and research that help accelerate the development of a coherent impact investing industry.
- The GIIN achieves this by:
  - Facilitating knowledge exchange
  - Highlighting innovative investment approaches
  - Building the evidence base for impact investing
  - Producing tools and resources
- The GIIN also produces databases:
  - **IRIS+** (of metrics for measuring and managing impact), and
  - **ImpactBase** (of impact investing funds).

Reporting Initiatives

Global Reporting Initiative (GRI)

- Publishes the GRI Standards, which provide guidance on disclosure across environmental, social and economic factors for all stakeholders, including investors, whereas the other major frameworks are primarily investor focused

CDP (formerly Carbon Disclosure Project)

- The CDP is a nongovernmental organisation (NGO) which supports companies, financial institutions and cities to disclose and manage their environmental impact

ESG Disclosure Framework of the **International Business Council (IBC)** aims to bring greater consistency and comparability to sustainability reporting by establishing common metrics for company disclosure.

Reporting Initiatives

Climate Disclosure Standards Board (CDSB)

- The CDSB is an international consortium of business and environmental NGOs with the mission to create the enabling conditions for material climate change and natural capital information to be integrated into mainstream reporting.

Corporate Reporting Dialogue (CRD)

- Corporate Reporting Dialogue (CRD) is a joint project led by the CDP, the Climate Disclosure Standards Board (CDSB), the Global Reporting Initiative (GRI), the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB).
- The 'Better Alignment Project' is focused on promoting better alignment in the corporate reporting landscape, making it easier for companies to prepare effective and coherent disclosures that meet the information needs of capital markets and society.

Other Initiatives

Asia Investor Group on Climate Change (AIGCC)

- An initiative to create awareness among Asia's asset owners and financial institutions about the risks and opportunities arising from climate change and low carbon investing

Reporting Initiatives

Value Reporting Foundation (VRF)

Formed by the merger of:

VRF's objective is to provide investors and corporates with a comprehensive corporate reporting framework across the full range of enterprise value drivers and standards.

The International Integrated Reporting Council (IIRC)

Created the Integrated Reporting Framework (IRF) that encourages companies to integrate sustainability within their strategy and risk assessment by integrating it into the traditional annual report

And

The Sustainability Accounting Standards Board (SASB) that created standards that are focused on the key material sustainability issues which affect 70-plus industry categories. Along with the SASB materiality maps, is particularly helpful for investors determining what is material for reporting and facilitates a more standardised benchmarking process

Reporting Requirements

The EU's Sustainable Finance Disclosure Regulation (SFDR)

- Designed to support institutional asset owners and retail investors to compare, select, and monitor the sustainability characteristics of investment funds by standardising sustainability disclosures
- Applies to all financial advisors and financial market participants that construct financial products and/or provide investment advice or insurance advice in the EEA
- Stipulates two levels of disclosure: firm level and product level
- Also introduces a new concept: Principal Adverse Impacts (PAIs) – the negative effects from an investment on sustainability factors

Answers to Sample Exam Questions

Question 1: **C** Pollution and resources

Question 2: **D** Value investment

Question 3: **A** Emerging and urban

Question 4: **D** Externality engagement

Question 5: **D** Facilitate knowledge exchange