

Fund ESG Weighted Average Metric (WAM)

Methodology

S&P Global Sustainable1 – April 2024

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Introduction

Fund Level Sustainability Analytics

Sustainability data provides financial institutions, corporations, and governments with expansive insight on business risk, opportunity, and impact as we work towards a sustainable future.

To empower financial institutions to unlock the power of sustainability insights, it is important that these data points can be associated with the issuers of financial instruments, across various asset classes. Mapping sustainability data, which is mainly researched at the parent or ultimate parent level, to subsidiaries provides an important link to equity and fixed income securities. Financial products, such as mutual funds and exchange traded funds (ETFs), may be analysed based on the sustainability data of the constituents of an investment vehicle.

This may provide financial institutions with tools to be able to analyse companies and deploy capital to enable a sustainable future.

It is important to note that these analytical metrics are not intended to be a score or a rating at the fund or financial security level. The creation of these metrics is systematic, and no expert opinion is incorporated into aggregation of the underlying sustainability data. It is critical to consider the underlying data points to complete a holistic assessment of the relevant portfolio companies.

Users of these analytics may choose to create their own methodology using the Portfolio Analytics tool within S&P Capital IQ Pro.

Methodology Overview

Financial Instrument Scope

Several assumptions are made in the computation of fund and security level sustainability analytics, using company level data:

1. Only physical positions are considered, synthetic positions are excluded.
2. Cash Equity and Corporate Fixed Income asset classes are only considered for the analysis of mutual funds and ETFs.
3. A subsidiary may inherit or use a sustainability data point from a parent or ultimate parent company, as a proxy.
4. Long funds only, short positions should be excluded and not be assessed.

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Materiality

The Fund ESG Weighted Average Metric (WAM) calculation's main inputs are the S&P Global ESG Scores, as described in the following sections.

The S&P Global ESG Scores consider double materiality as the foundation of the methodology. For more information, please see the [S&P Global ESG Scores page](#).

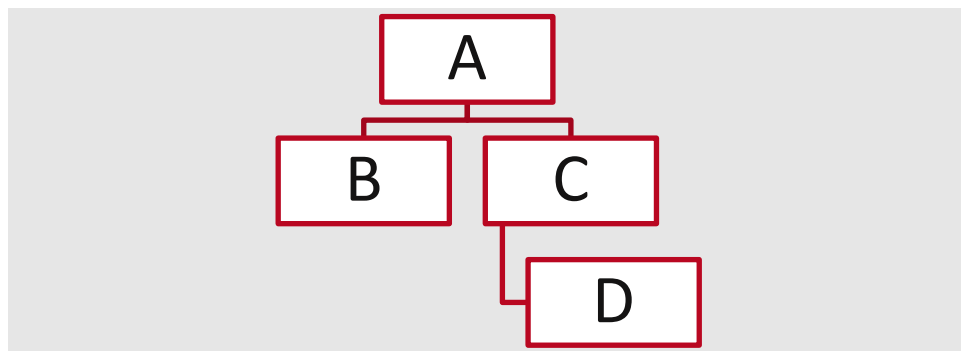
Mapping of ESG Scores to Financial Instruments

The coverage of ESG scores is limited when compared to the investible universe of companies. Hence, it is important to establish valid relationships to determine when an ESG score may be applicable to other companies, for example inherited from a parent company. For this purpose, the S&P Global Market Intelligence corporate hierarchy data has been used.

The inheritance of an ESG score from a parent company to a subsidiary is generally permitted when all the following conditions are met:

1. The parent company is the majority owner (with >50% ownership) of the subsidiary, and is the controlling parent.
2. The subsidiary is not a distinct operating entity, **meaning that it doesn't operate independently** of the parent company and reports under the same reports.
3. The subsidiary is not a fund.
4. The parent company has an ESG score that was researched in the past three years.

Figure 1: A worked example: ESG Scores



- A and C have ESG scores.
- B is a subsidiary of A, so can inherit the ESG score of A. This is because A has control over the operations of B and more than 50% ownership.
- C is a distinct operating entity from A, and therefore does not inherit A's score. It is researched independently and has its own ESG score.
- D is a subsidiary of C, so can inherit the ESG score of C.

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This inheritance logic applies for the Fund ESG WAM aggregation logic.

Preparing the Portfolio

Several steps are taken to prepare the data for computation:

1. Holdings without sustainability data point coverage are dropped
2. The portfolio is re-weighted such that the portfolio weights sum to 100%, per the below formula:

$$W_{new,i} = \frac{w_{old,i}}{\sum_{i=1}^n w_{old,i}} \text{ for } i \text{ holdings in a portfolio that have sustainability data}$$

A worked example: ESG Scores

- a. A portfolio has the following composition, as per its latest filing.

Holding	Portfolio Weight (%)	ESG Score Available?	ESG Score
Stock 1	50%	Y	80
Stock 2	20%	Y	70
Stock 3	25%	Y	60
Stock 4	3%	Y	50
Stock 5	2%	N	-

- b. To conduct fund level sustainability analytics, the holding with no ESG score is dropped

Holding	Portfolio Weight Before Reweight (%)	Portfolio Weight After Reweight (%)	ESG Score Available?	ESG Score
Stock 1	50%	51.0%	Y	80
Stock 2	20%	20.4%	Y	70
Stock 3	25%	25.5%	Y	60
Stock 4	3%	3.1%	Y	50

- c. The reweighted portfolio weight is used to calculate analytics for ESG score fund level analytics

Weighted Average Metric (WAM) Calculation

S&P Global uses a simple weighted average as the default metric to provide an indication of the sustainability profile for the issuing companies within a portfolio.

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In the case of ESG scores, the following formula is used to calculate the fund level metric:

$$\text{Fund ESG WAM} = \frac{\sum_{i=1}^n w_{new,i} ESG_i}{\sum_{i=1}^n w_{new,i}} \text{ for } i \text{ holdings in a portfolio that have sustainability data}$$

Where w_i is the weight of the position in the reweighted portfolio and ESG_i is the ESG score associated with the relevant financial security.

The same calculation happens to calculate the Dimension level metrics:

$$\text{Fund ESG WAM}_D = \frac{\sum_{i=1}^n w_{new,i} (ESG_{D,i} * w_{D,i})}{\sum_{i=1}^n w_{new,i}}$$

For holding i in a portfolio, that has sustainability data, and dimension D between E, S and G.

Where w_i is the weight of the position in the reweighted portfolio, $ESG_{D,i}$ is the ESG score of dimension D associated with the relevant financial security and $w_{D,i}$ is the weight of dimension D for holding i .

A worked example: ESG Scores

Holding	Portfolio Weight Before Reweight (%)	Portfolio Weight After Reweight (%)	ESG Score	Contribution of Holding Fund ESG WAM
Stock 1	50%	51.0%	80	40.82
Stock 2	20%	20.4%	70	14.29
Stock 3	25%	25.5%	60	15.31
Stock 4	3%	3.1%	50	1.53
			TOTAL	71.94

In the case of the portfolio used in the example, the portfolio weight after rebalancing is multiplied by the ESG score of the position. The sum of these metrics creates a Fund ESG Weighted Average Metric (WAM) of 71.94 for the fund.

Users of these analytics may choose to create their own methodology and relevant metrics using the Portfolio Analytics tool within S&P Global Capital IQ Pro, to suit their individual requirements. A wide selection of equity mutual funds, fixed income mutual funds and ETFs can be selected. Alternatively, a portfolio can be uploaded or created to compute sustainability fund and security level analytics.

Monitoring and Review

All new methodologies and any material changes to existing methodologies are reviewed and approved by an independent methodology governance committee.

Updates

We periodically review our methodology as appropriate.

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