

Internet Appendix A120: Sustainability Investing

A120.1 Illustrative Reverse Engineered Pitch Template Example

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(A) Working Title	Lee, D., Faff, R. and S. Rekker, "Do High and Low-ranked Sustainability Stocks Perform Differently?", International Journal of Accounting and Information Management, Vol. 21, No. 2, 2013, pp. 116-132.				
(B) Basic Research Question	Is there a significant difference in the risk-adjusted performance between high- and low-ranked corporate social performance (CSP) firms?				
(C) Key paper(s)	1. Derwall, J.N., Koedijk, K. and Ter Horst, J. (2011), "A tale of values-driven and profit-seeking social investors", Journal of Banking & Finance, Vol. 35, pp. 2137-2147. 2. Lee, D.D. and Faff, R.W. (2009), "Corporate sustainability performance and idiosyncratic risk: a global perspective", Financial Review, Vol. 44, pp. 213-237. 3. Derwall, J.N., Guenster, N., Bauer, R. and Koedijk, K.C.G. (2005), "The ecoefficiency premium puzzle", Financial Analysts Journal, Vol. 61, pp. 51-63.				
(D) Motivation/Puzzle	The environmental, social and governance (CSG) factors have been widely considered during the process of designing investment portfolio. However, there has been little analysis of the impact of ESG factors on stocks performance in the US. Most previous US studies measure CSR by employing KLD dataset from which individual company rankings are not available and some 'sin' industries are excluded. To fill up the research gap and to overcome the shortcoming of KLD data, the authors use ESG/CSP ratings, applicable to all industries, to examine the impact of CSP factors upon stock performance in the US stock market.				
THREE	Three core aspects of any empirical research project i.e. the " IDioTs " guide				
(E) Idea?	The core idea is to segregate the US firms into different CSP portfolios based on their ESG/CSP ratings and then to test whether there is a significant difference in the risk-adjusted stock performance between the high- and low-ranked CSP stocks.				
(F) Data?	The data employed are ESG/CSP ratings generated by Sustainability Asset Management Group GmbH (SAM), over the period 1998-2007. Besides, all firms that comprise the US components of the SAM's database covering the same period are matched against those firms represented in the CRSP stock database. Firm size, price-relatives, industry codes, and monthly market returns data are sourced from the CRSP data-files.				
(G) Tools?	The high- and low-ranked CSP firms are compared with each other under two separate groups, leading and lagging CSP industries, with regard to mean return, SD, R/R ratio, Sharpe ratio, M squared and Beta. Besides, the Fama-French Model augmented by momentum and industry factors is implemented primarily to test the significance of the alpha for CSP difference portfolios, defined as high-ranked minus low-ranked CSP stocks. The first CSP difference portfolio is grouped under the leading and the lagging industry. The second is the high and low CSP "conviction" portfolio that comprises 30 firms with the highest/lowest CSP scores as derived from the entire sample. And the third is Best of Sector (BOS) and Worst of Sector (WOS) CSP portfolio that consists of 30 very best and very worst CSP ranked firms within each industry. The significance of the Alpha under the three scenarios is obtained respectively.				
TWO	Two key questions				
(H) What's New?	The research sheds a new light in the examination of the impact of CSP factors on stocks performance in the US market because of the employment of ESG/CSP rating, instead of KLD dataset used by the previous US related studies.				
(I) So What?	The benefit of employing ESG/CSP ratings is evident. First, it does not exclude some firms engaged in alcohol, tobacco, firearms, gambling, nuclear power and military weapons. Thus, there is more comparable information with the use of ESC/CSP ratings. Second, the SAM ratings process is largely congruent with the UN PRI, which continues to experience unprecedented growth in assets managed according to these environmental, social, and governance factors. Finally, the individual ratings data allow the formation of both BOS and WOS ESG portfolios that enable to test the difference in performance regardless industry specific factors.				

ONE	One bottom line
(J) Contribution?	The results are consistent with the “no-linkage” hypothesis, which argues that no significant difference in the risk-adjusted performance is expected between high- and low-ranked CSP-formed portfolios. The tuition and indication is that there is neither a material financial cost nor benefit afforded to ESG investing. This conclusion is also consistent with arguments presented in Derwall et al. (2011) – there is a heterogeneous group of investors and profit-driven investors employing positive screening have diminished the profit-generating opportunities over time. Besides, this research can significantly contribute to better portfolio management. On the one hand, investing according to ESG criteria does not prohibit active investors from seeking Alpha. On the other hand, passive investors can invest in ESG portfolios without penalty. Long-term investors are able to incorporate ESG factors into their ongoing investment processes without sacrificing returns.
(K) 3 Key Findings	<ol style="list-style-type: none"> 1. No significant difference in the risk-adjusted performance is expected between high- and low-ranked CSP-formed portfolios. 2. Little evidence is found to suggest that high- or low-ranked CSP-formed portfolios, irrespective of portfolio formation type, systematically differ with regard to performance, size, book-to-market, or momentum factors. 3. The US equity market is, in the main, efficient with regard to material sustainability risks and rewards.

