5 May 2018

Il Sole 24Ore

ANALYSIS ON THE STOXX EUROPE 600 INDEX

Good guys win in the stock exchange: "responsible shares" earn more

by Enrico Marro

Being good is its own reward. The market rewards "good, responsible shares" – the ones earning the highest ratings from an environmental, social or governance perspective – more than other shares. That is what emerges from the first European study on the correlation between environmental, social and governance (ESG) rating and stock performance. The study was conducted by the School of Management of Politecnico di Milano and Banor SIM, using the same methodology as used by Harvard Business School to analyse the US market.

The research focused on the performance of companies in the Stoxx Europe 600 index from 2012 to 2017. The index includes 600 high, medium and low-cap companies from 17 European countries. The number of companies actually analysed was 882, because during the six years of the analysis the composition of the Stoxx 600 index changed occasionally.

For each security, data were collected on stock market prices, operational performance as reported in financial statements and non-accounting information concerning ESG parameters. The last-named was based on Thomson Eikon ESG data, which include 424 annual indicators available for each company and grouped in 10 categories. The basket does not include stocks that are not included in the ESG rating, such as arms producers.

The results reward the stocks of the companies that are most responsible from an ESG perspective. Stocks belonging to the quartile of companies with the highest ESG ratings are the ones that perform best and show a higher growth in earnings and better margins. Indeed, integrating ESG indicators and the classic economic-financial considerations used by analysts adopting a value-based approach (as followed, for example, by Warren Buffett) is, according to the study, the best strategy to create efficient portfolios. Especially as regards returns, because in terms of yield volatility no major differences emerged between "good" and not-so-good stocks.

All of this could create a virtuous circle, as Prof. Giancarlo Giudici of the School of Management of Politecnico di Milano notes. Integrating ESG sustainability criteria and considering all stakeholders, using the traditional models of value-based financial analysis, can benefit both fund managers and investors.

"**It's important to recognise that a correlation does indeed exist** between best performers and the adoption of ESG principles", underscores Massimilano Cagliero, founder and CEO of Banor SIM, "even if today in the United States this correlation is also driven by flows. The hope is that all of this triggers a virtuous circle in the real economy, with a resulting push for listed companies to adapt in order to attract investors". Because people who become more virtuous in the stock markets eventually discover they've also become richer.