

# ESG Data Signals

## S&P Global ESG Scores



### Highlights

- Using the S&P Global ESG score, investors can optimize the environmental, social and governance tilts of portfolios.
- Using the S&P Global ESG Score as a constraint in portfolio alignment the weighted S&P Global ESG Score of an ESG Tilted S&P 500 and ESG Tilted MSCI portfolio increases by an average of 24% as compared to the benchmark, whilst still largely maintaining the underlying benchmark characteristics.
- From January 2014 to July 2020, the S&P 500 went up 113%. In that same time period, our ESG titled S&P 500 portfolio increased 121%, a difference of 8.5% over that time. Since the Covid outbreak in March 2020, the S&P 500 is up 13.2%, while the ESG tilted S&P 500 portfolio grew 15%, a difference of 1.8%.

### Authors

#### Liam Hynes

EMEA Head,  
Capital Markets  
Product Specialists

S&P Global  
Market Intelligence

#### Ruben Falk

Global Head,  
Investment Management  
Product Management

S&P Global  
Market Intelligence

---

**S&P Global**

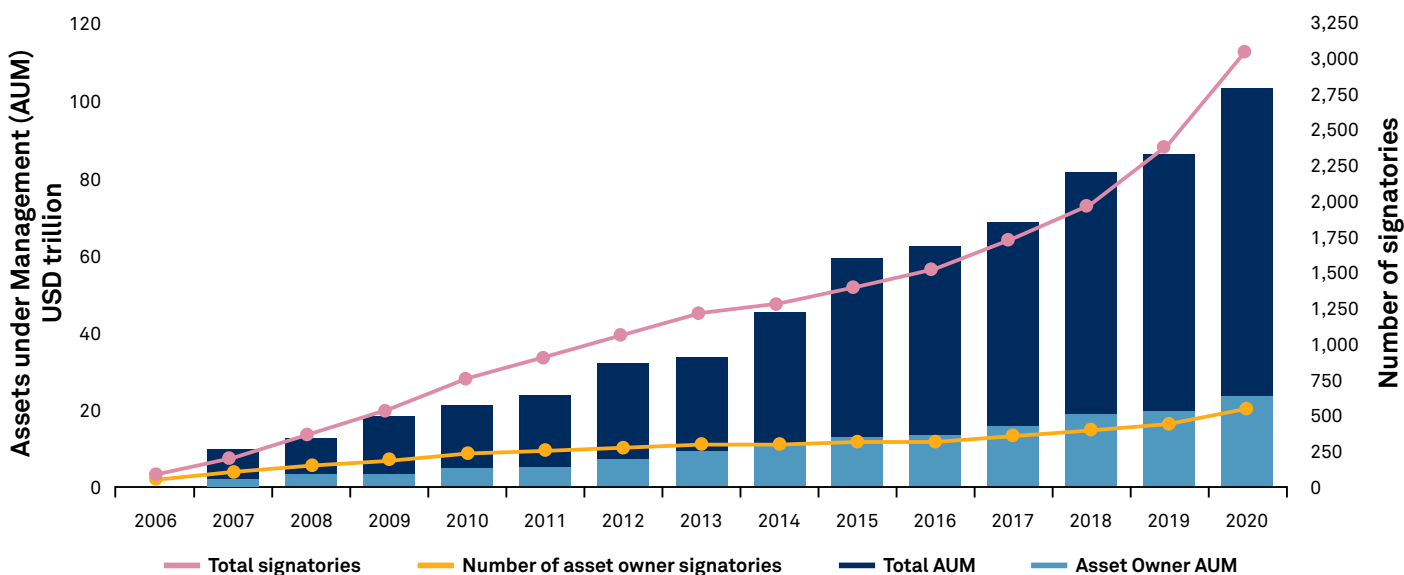
Market Intelligence

# Environmental, social and governance considerations

The trend towards increasing integration of Environmental, Social and Governance (ESG) considerations in investment decision making is a growing feature of financial markets. Total assets invested using ESG principles globally has risen by 34% from 2016 to 2018, amounting to approximately \$30.7 trillion at the start of 2018.<sup>1</sup>

A further benchmark of growing commitment to ESG factors in investment decision making and ownership, is found in the number of organizations signing up to the United Nations backed Principles for Responsible Investment (PRI). As of September 2020, the PRI counts >3,000 signatories with USD 103 trillion assets under management (AUM), up from just 63 signatories with USD 6.5 trillion AUM in 2006 (Figure 1).

Figure 1: PRI Growth: 2006-2020



Source: PRI, 2020. Data accessed at Sept, 2020.

## The implications of the global pandemic

The global pandemic put a spotlight on the value of ESG considerations in capital markets. Global sustainability indices outperformed mainstream market benchmarks and between April and June, ESG investments achieved record inflows, pushing assets under management to a new high of more than \$1tn.<sup>2</sup> Through September, the S&P 500 ESG Index outperformed the S&P 500 by 2.5% and the S&P 500 Paris-Aligned Climate Index outperformed the S&P 500 by 5.57% in that same time.

The global pandemic highlighted the importance of businesses who accounted for ESG factors, as they were likely better prepared to both weather such crises and operate in a post-crisis world. These businesses tend to be better-managed companies, with stronger competitive advantages, healthier balance sheets, and a better social license to operate than their non-ESG peers.<sup>3</sup>

1 Global Sustainable Investment Alliance. Trends Report 2018. Retrieved from GSI website: <http://www.gsi-alliance.org/trends-report-2018/>  
 2 Morningstar, August 4 2020: Sustainable Fund Flows Hit Record in Q2  
 3 Dornau, Robert. S&P Global: The Evolution of Sustainable Investing Rewards, 2020

# S&P Global ESG Scores

The S&P Global ESG Scores were made accessible to the global investment community on 18th May 2020.

Powered by the SAM Corporate Sustainability Assessment, acquired by S&P Global at the end of 2019, S&P Global ESG Scores are based on a methodology that was built by investment practitioners with investment processes in mind. In SustainAbility's Rate the Raters 2019 report, companies rated the CSA as the most useful ESG assessment thanks to its high level of transparency, its sector-specific view of material ESG issues, and its forward-looking incorporation of emerging sustainability risks and opportunities.<sup>4</sup> In the 2020 report, which looked at the investor perspective, the CSA came out top among the highest-quality ratings and was cited as a "strong signal of sustainability."<sup>5</sup>

The approach of S&P Global ESG Scores focuses on financially relevant material factors in each industry drawing on more than two decades of engaging with thousands of companies through the CSA. With coverage of 7,300 companies representing approximately 95% of global market capitalization, S&P Global ESG Scores give financial institutions the flexibility to drill down into three underlying Environmental, Social and Governance & Economic Dimension Scores, and an average of 23 Criteria Scores. A 100-question exploration (average), guided by 61 industry-specific approaches, informs each criteria score. The ESG Scores are from 1 to 100, with 100 being ranked the best.

## Aligning portfolios with S&P Global ESG Scores




*Can we use S&P Global's ESG Score as the objective by which to optimize a portfolio to generate greater ESG alignment whilst still maintaining the characteristics of the underlying benchmark?*

Those characteristics namely being:

-  Sector & Country Exposures
-  Beta Exposure

We constructed ESG tilted portfolios based on the S&P 500<sup>®</sup> and the MSCI World using the following parameters:

**Maximize portfolio weighted average ESG Score subject to the constraints of:**

-  Sector & Country Exposure Neutrality
-  Beta Neutrality
-  50% – 200% Individual Holding Weights Relative to the Benchmark

<sup>4</sup> Wong, Christina, et al. Rate the Raters 2019: Expert Survey Results. SustainAbility, an ERM Group company, 2019, pp. 1–39

<sup>5</sup> Wong, Christina, and Erika Petry. Rate the Raters 2020: Investor Survey and Interview Results. SustainAbility, an ERM Group company, 2020, pp. 1–54

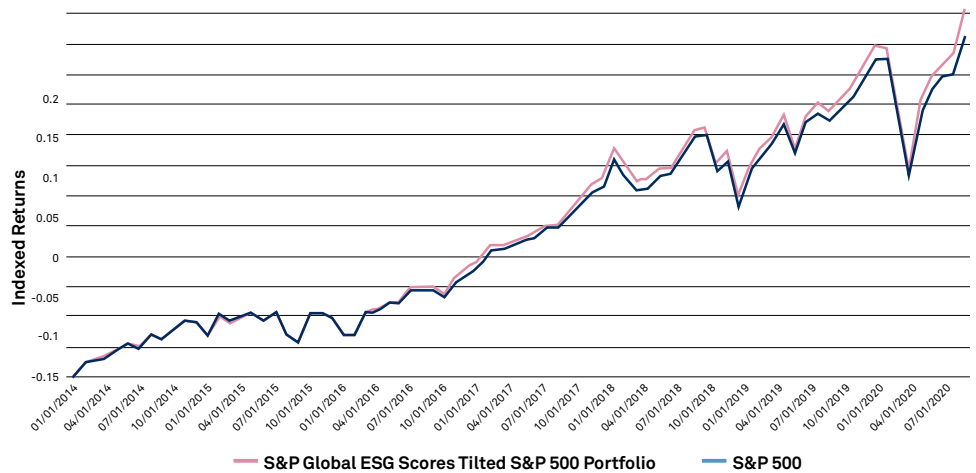
# ESG Portfolio Results

The ESG titled portfolio we constructed from the S&P 500 maintains the underlying S&P 500 characteristics<sup>6</sup> without significantly differing from the return profile of the benchmark. The realized tracking error of the portfolio is 1.6%. From January 2014 to July 2020, the S&P 500 went up 113%. In that same time period, our ESG titled S&P 500 portfolio increased 121%, a difference of 8.5% over that time. Since the Covid outbreak in March 2020, the S&P 500 is up 13.2%, while the ESG tilted S&P 500 portfolio grew 15%, a difference of 1.8%.

Similarly, the ESG titled portfolio constructed from the MSCI World maintains the underlying MSCI World characteristics<sup>7</sup> without any significant impact on the return profile. The realized tracking error of the portfolio is just 1.3%.

Please note that all historical back-test performance figures in this brief exclude fees and transaction costs.

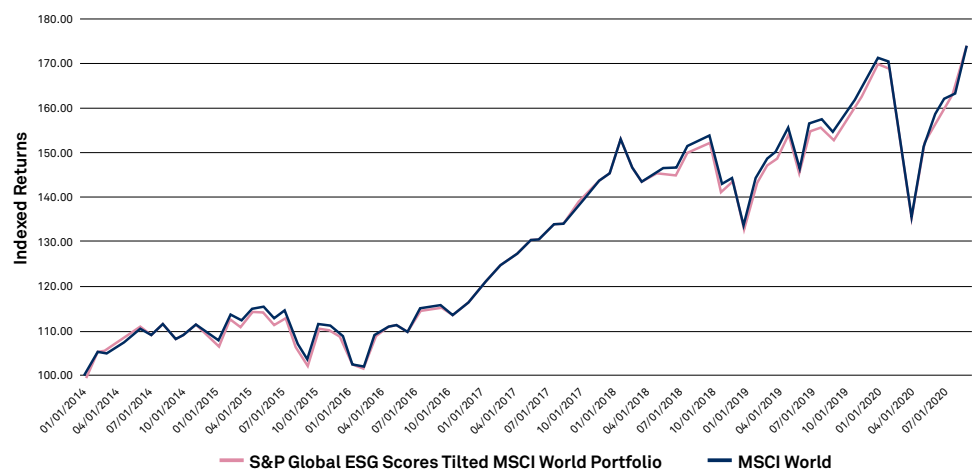
**Figure 3: S&P Global ESG Scores Tilted S&P 500 Portfolio vs S&P 500® Returns**



Source: S&P Global ESG Scores. Current as at August 31, 2020.

Indices are unmanaged, statistical composites and their returns do not include the payment of any sales charges or fees an investor would pay to purchase the securities they represent. It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

**Figure 4: S&P Global ESG Scores Tilted MSCI World Portfolio vs MSCI World Returns**



Source: S&P Global ESG Scores. Current as at August 31, 2020.

Indices are unmanaged, statistical composites and their returns do not include the payment of any sales charges or fees an investor would pay to purchase the securities they represent. It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

6 Beta, Country & Sector Neutral, Tracking Error: 1.57%, Sharpe Delta: -0.011, Annualized rate of return 12.88% vs S&P 500 of 12.96%  
 7 Beta, Country & Sector Neutral, Tracking Error: 1.3%, Sharpe Delta: -0.007, Annualized rate of return 8.83% vs MSCI World of 9.34%

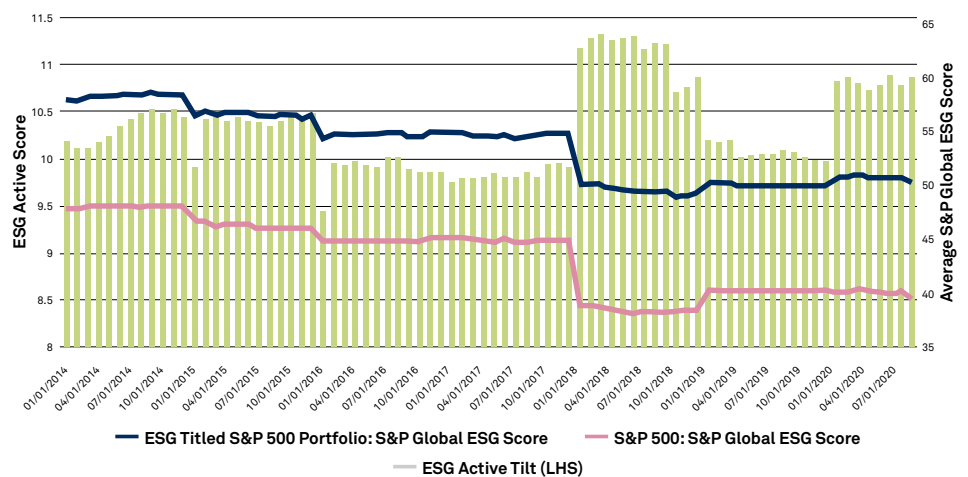
# ESG Characteristics

Knowing that we can use the ESG Score as the objective in the portfolio alignment and that we still track the respective benchmarks quite closely, what are the resulting ESG profiles of the ESG tilted S&P 500 & MSCI World portfolios?

The S&P 500 over the past 6 years had a weighted average ESG Score of 43.4<sup>8</sup> whereas the average score of the ESG tilted S&P 500 stood at 53.7,<sup>9</sup> an average increase in the ESG Score of 10.3 or 24% as compared to the benchmark whilst still largely maintaining the underlying S&P 500 characteristics.

The MSCI World over the past 6 years had an average ESG Score of 48.8<sup>10</sup> whereas the average score of the ESG tilted MSCI World stood at 63.3,<sup>11</sup> an average increase in the ESG Score of 11.5 or 24% as compared to the benchmark whilst still largely maintaining the underlying MSCI World characteristics.

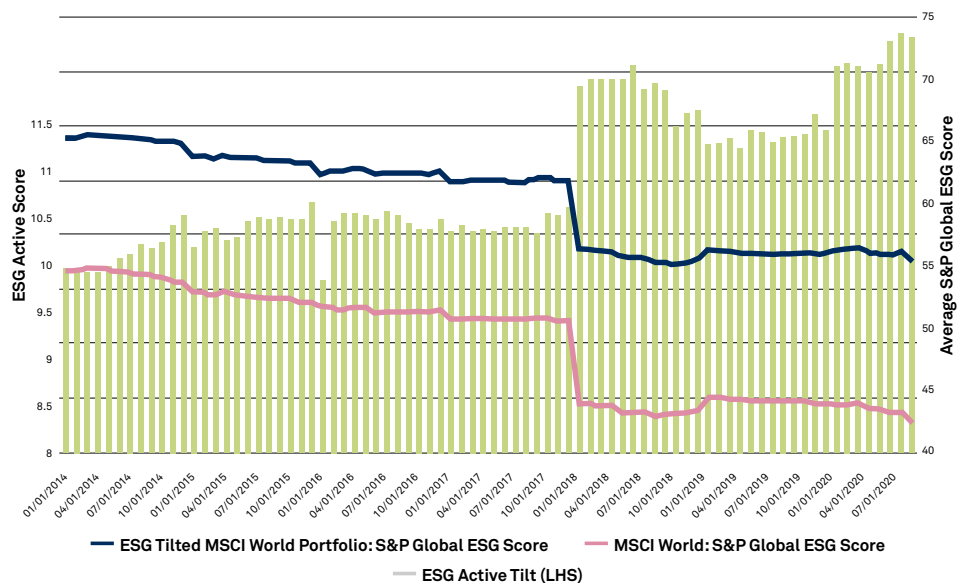
**Figure 5: ESG Active Tilt – Portfolio vs S&P 500®**



Source: S&P Global ESG Scores. Current as at October 2020.

Indices are unmanaged, statistical composites and their returns do not include the payment of any sales charges or fees an investor would pay to purchase the securities they represent. It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

**Figure 6: ESG Active Tilt – Portfolio vs MSCI World**



Source: S&P Global ESG Scores. Current as at October 2020.

Indices are unmanaged, statistical composites and their returns do not include the payment of any sales charges or fees an investor would pay to purchase the securities they represent. It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

8 SPGMI Weighted average S&P 500 ESG Score, The overall drop in scores between 2017 and 2018 is the result of a major review of the CSA Media and Stakeholder Analysis (MSA) approach that considers the impact of corporate controversies in the ESG score calculation. For more information click [here](#).  
 9 SPGMI Weighted average ESG Constructed S&P 500 Portfolio ESG Score  
 10 SPGMI Weighted average MSCI World ESG Score  
 11 SPGMI Weighted average ESG Constructed MSCI World Portfolio ESG Score



# Summary

We illustrate a sample framework for aligning ESG factors into the portfolio construction process, highlighting that these ESG considerations need not necessarily be distinct from thinking about portfolio performance.

When applying an ESG framework to the portfolio construction process, the initial reaction may be to screen out the worst scoring companies and construct a portfolio from the remaining universe. However this exclusionary process can cause the resulting portfolio to drift from the benchmark's characteristics.

The framework outlined here shows that it is possible to incorporate ESG scores into the portfolio construction process while not sacrificing the desired portfolio characteristics. This can likely be extended to using ESG as an overlay to other existing strategies.

# References

1. Global Sustainable Investment Alliance. Trends Report 2018.  
Available at: <http://www.gsi-alliance.org/trends-report-2018/>
2. Morningstar, August 4 2020: Sustainable Fund Flows Hit Record in Q2
3. Dornau, Robert. S&P Global: The Evolution of Sustainable Investing Rewards, 2020
4. Wong, Christina, et al. Rate the Raters 2019: Expert Survey Results. SustainAbility, an ERM Group company, 2019
5. Wong, Christina, and Erika Petry. Rate the Raters 2020: Investor Survey and Interview Results. SustainAbility, an ERM Group company, 2020
6. MSA Methodology Guidebook 2020: SAM Corporate Sustainability Assessment (CSA).  
Available at: [https://portal.csa.spglobal.com/survey/documents/MSA\\_Methodology\\_Guidebook.pdf](https://portal.csa.spglobal.com/survey/documents/MSA_Methodology_Guidebook.pdf)

**For more information visit**

**[www.spglobal.com/marketintelligence/esg](http://www.spglobal.com/marketintelligence/esg)**

## CONTACTS

### **The Americas**

+1 800 402 8774

[Trucostnorthamerica@spglobal.com](mailto:Trucostnorthamerica@spglobal.com)

### **Europe, Middle East & Africa**

+44 (0) 20 7160 9800

[Trucostinfo@spglobal.com](mailto:Trucostinfo@spglobal.com)

[TrucostEMEA@spglobal.com](mailto:TrucostEMEA@spglobal.com)

### **Asia-Pacific**

+65 6597 6158

[Trucostasiapacific@spglobal.com](mailto:Trucostasiapacific@spglobal.com)

[www.spglobal.com/marketintelligence](http://www.spglobal.com/marketintelligence)

Copyright © 2020 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

These materials have been prepared solely for information purposes based upon information generally available to the public and from sources believed to be reliable. No content (including index data, ratings, credit-related analyses and data, research, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of S&P Global Market Intelligence or its affiliates (collectively, S&P Global). The Content shall not be used for any unlawful or unauthorized purposes. S&P Global and any third-party providers, (collectively S&P Global Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Global Parties are not responsible for any errors or omissions, regardless of the cause, for the results obtained from the use of the Content. THE CONTENT IS PROVIDED ON "AS IS" BASIS. S&P GLOBAL PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Global Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

S&P Global Market Intelligence's opinions, quotes and credit-related and other analyses are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P Global Market Intelligence may provide index data. Direct investment in an index is not possible. Exposure to an asset class represented by an index is available through investable instruments based on that index. S&P Global Market Intelligence assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P Global Market Intelligence does not act as a fiduciary or an investment advisor except where registered as such. S&P Global keeps certain activities of its divisions separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain divisions of S&P Global may have information that is not available to other S&P Global divisions. S&P Global has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.