University of Zurich[UZH]

How Do Sustainable Investments Perform?

Hans-Luzi Fausch

Master's Thesis

Professor Dr. Marc Chesney
University of Zurich
Department of Banking and Finance
Plattenstrasse 32
CH-8032 Zurich
Tel: +41 634 41 07

Abstract

A constant notion that has shaped the economy over the past two decades is the term "sustainability". Consequently, every company must deal with environmental, social and governmental (ESG) issues. A relatively recent trend is an investment strategy with the focus on sustainable companies. As such an investment strategy becomes increasingly important, the companies must also increasingly move towards sustainable investment.

This thesis examines the contrast in performances by the Swiss Market Index (SMI) and a Sustainable Index consisting of the SMI's most sustainable companies. This comparison provides insight into the performance of an index that has solely financial criteria and one that has additional sustainable criteria. Any differences in performance can therefore be seen as the result of the sustainable effect. The selection of the sustainable companies was based on the Sustainable Development Goals (SDGs), which were established by the United Nations in 2015. In a further step, the thesis analyses whether sustainable indices perform better than an index consisting of companies with bad ESG scores.

Analysis of the cumulative returns of the SMI and the new created Sustainable Index shows clear evidence that the Sustainable Index should be preferred. Apart from a few exceptions, the hypothesis that sustainable investment is the dominant strategy is consistently supported by the Sharpe Ratio, the Treynor Ratio and the Jensen Ratio calculation. Furthermore, the Sustainable Index has lower systematic risk and lower total risk. On the contrary, due to the high correlation between the two indices, a two-sided t-test calculation could not deliver a significant difference in the monthly return rate between the two indices. The results of the comparison between the Bad ESG Index and other sustainable indices are also clearly in favour of a sustainable investment strategy. The Bad ESG Index has the lowest cumulative returns, together with the lowest Sharpe Ratio and Treynor Ratio. Furthermore, it is the only index with a negative Jensen Ratio. While the systematic risk analysis delivers no clear results as to whether the Bad ESG Index or the sustainable indices should be preferred, the results of the total risk analysis are clearly in favour of the sustainable indices. However, there was also no perceptible significance found as to the difference of the monthly return rate when comparing the Bad ESG Index and the sustainable indices.