Exploring the Incorporation of ESG Investment for SRI in Qatar

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Introduction

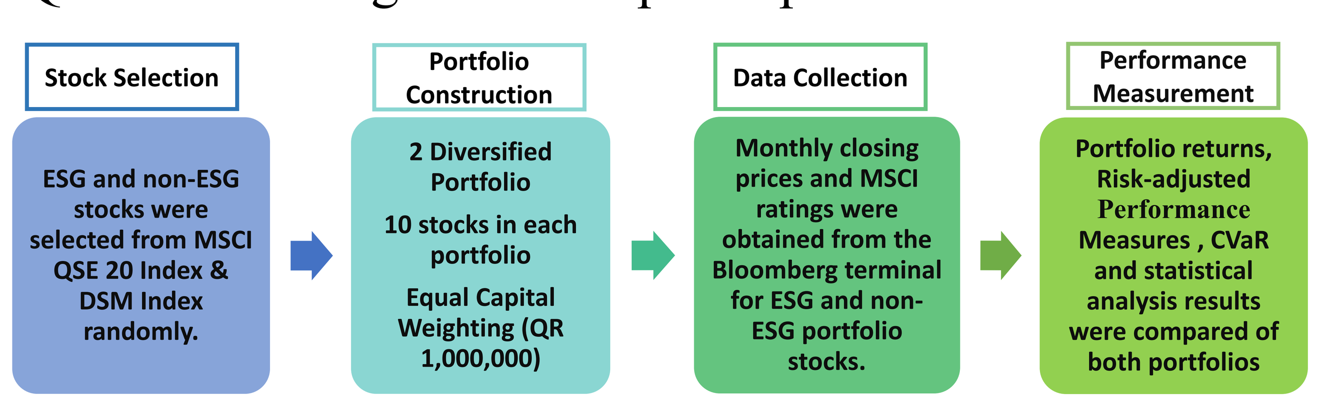
In a move towards a sustainable future, Qatar Stock Exchange and MSCI introduced the "MSCI QSE 20 ESG Index" in November 2021 combining ESG factors to provide financial returns and help achieve Qatar's climate and sustainability goals.

Hence, this research aims to explore the current initiative of incorporation of ESG criteria in portfolio performance and assess the risk and opportunities associated with ESG investments for Socially Responsible Investment, which can be achieved by:

- **Comparing MSCI QSE 20 Index stock returns with Qatar Stock Exchange (DSM Index) stock returns**
- **Examine if ESG stocks yields profits for investors**
- **Recommend Strategies for responsible investors for ESG investments**

Methodology

This research is exploratory in nature and aims at contributing further research on the implications of SRI and ESG integration for the transition towards sustainable development in Qatar. Following are the steps for portfolio construction.

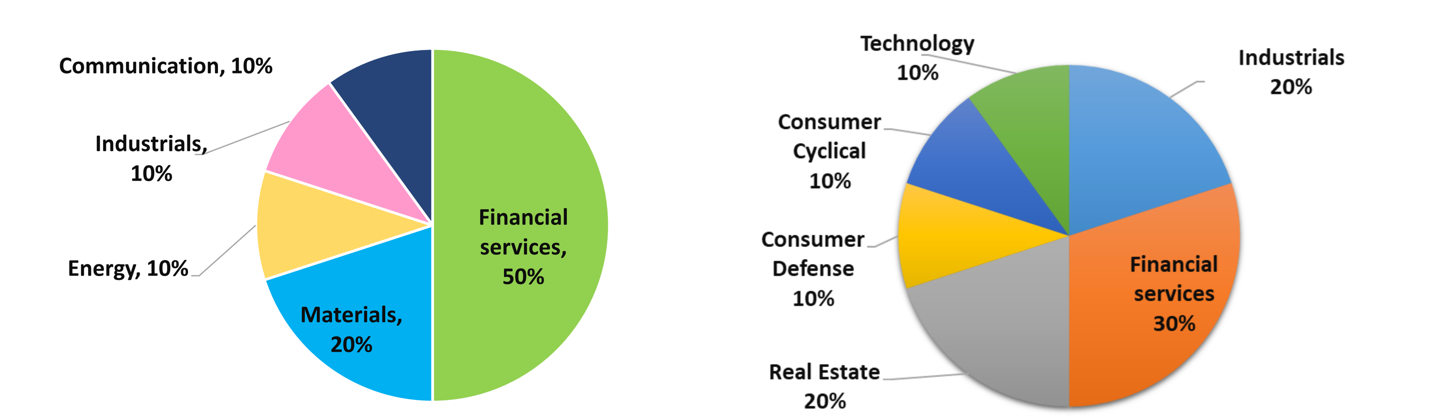


ESG Portfolio Holdings and their MSCI Ratings

Stocks	Ticker	Sector	Environmental	Social	Governance	MSCI Rating	Risk Score	Risk Category
Al Ahli Bank	ABQK	Financial Services	0.00	0.23	3.47	-	-	-
Commercial Bank of Qatar	CBQK	Financial Services	0.00	1.15	3.44	BBB	27.72	Medium
Doha Bank	DHBK	Financial Services	0.00	1.29	3.47	-	-	-
Industries Qatar	IQCD	Materials	0.09	1.27	2.93	B	41.27	Severe
Mesaieed Petrochemical	MPHC	Materials	0.17	4.06	2.40	CCC	30.13	High
Ooredoo	ORDS	Communication Services	7.40	12.60	8.50	BBB	28.5	Medium
Qatar Fuel Company	QFLS	Energy	0.00	0.00	0.00	A	23.26	Medium
Qatar Gas Transport Company Limited (Nakilat)	QGTS	Industrials	0.91	4.28	3.90	BBB	21.43	Medium
Qatar Islamic Bank	QIBK	Financial Services	1.70	11.60	14.50	B	27.8	Medium
Qatar National Bank	QNBK	Financial Services	1.30	9.30	11.80	A	22.4	Medium

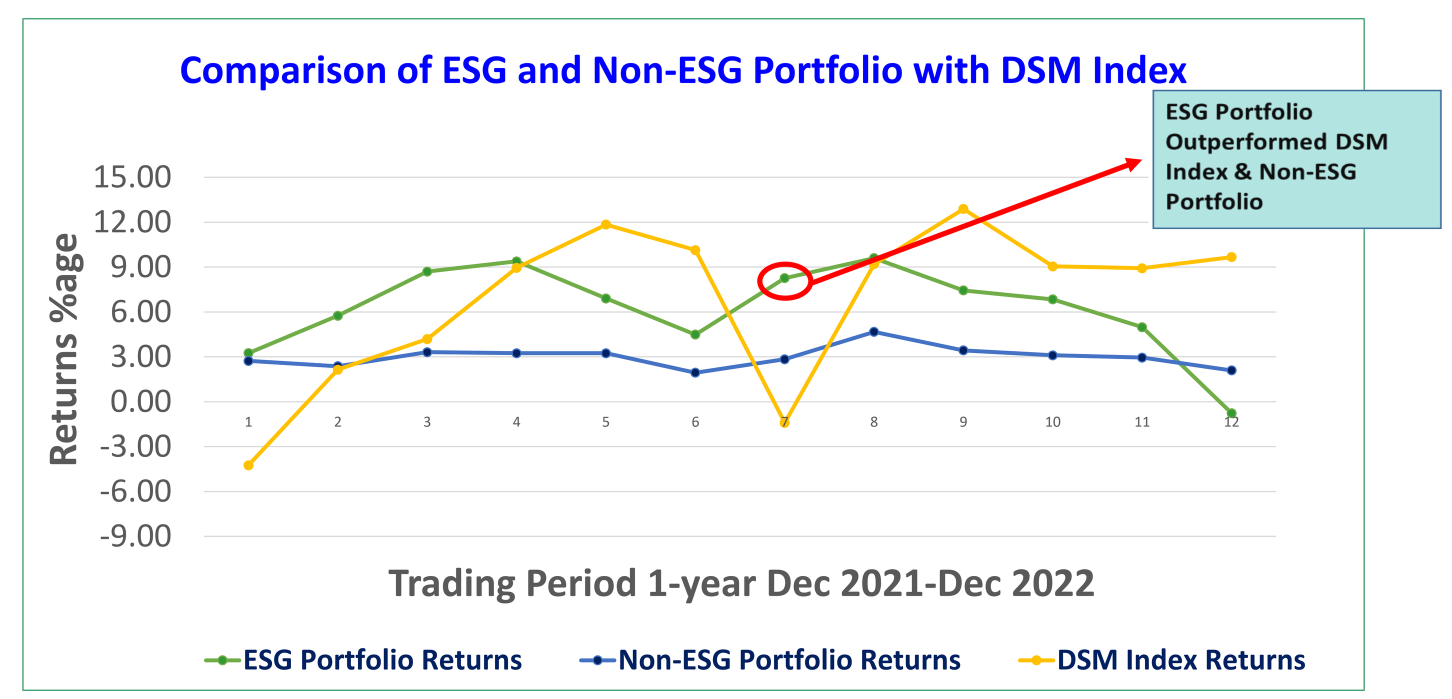
Non-ESG Portfolio Holdings.

Stocks	Ticker	Sector
Aamal Company	AHCS	Industrials
Al Khaleej Takaful Insurance Company	AKHI	Financial Services
Baladna	BLDN	Consumer Defense
Dlala Brokerage and Investment Holding Company	DBIS	Financial Services
Ezdan Holding Group	ERES	Real Estate
Mannai Corporation	MCCS	Technology
Al Meera Consumer Goods Company	MERS	Consumer Cyclical
Mekdam Holding Group	MKDM	Industrials
Mazaya Real Estate Development	MRDS	Real Estate
Lesha Bank LLC	QFBQ	Financial Services



Results

The graph compares ESG and Non-ESG overall portfolio returns for 1-year trading period. The ESG portfolio outperformed both non-ESG portfolio and the DSM Index at times, with returns ranging from 9.60% to -0.77%, while non-ESG portfolio showed continuous lower returns, but remained positive.



Statistical analysis is shown for both portfolios. Paired t-stat analysis for both portfolios were measured against the benchmark return. Mean and Standard deviation is higher for ESG portfolio (high risk, high return).

Portfolio	Mean (M)	Standard Deviation (SD)	t-stat
ESG	6.23% ↑	2.96% ↑	4.35 ↑
Non-ESG	2.98% ↓	0.71% ↓	2.06 ↓

Key performance indicators

Risk-adjusted Performance Measures	ESG Portfolio	Non-ESG Portfolio
EXCESS RETURN	1.95%	-1.35%
BETA	0.20%	0.08%
SHARPE	0.66%	-1.79%
TREYNOR	0.09%	-0.17%
JENSEN ALPHA	0.06%	0.03%
INFORMATION RATIO	1.26%	0.63%
MODIFIED SHARPE RATIO	0.66%	0.00%
SORTINO RATIO	0.55%	-1.01%
OMEGA RATIO	24.39%	-2.98%
CERTAINTY EQUIVALENT RETURNS (2)	6.11%	-0.97%
CERTAINTY EQUIVALENT RETURNS (3.5)	21.78%	-1.00%
CERTAINTY EQUIVALENT RETURNS (5)	74.72%	35.12%
CVAR	27,962	4,664
IDIOSYNCRATIC OR RESIDUAL RISK	9.21%	2.02%

According to the risk-reward principle, higher risk leads to higher rewards. Overall, the ESG portfolio showed positive risk-adjusted performance compared to the non-ESG portfolio, suggesting better return.

Portfolio Value

Portfolio	Portfolio Value (at Beginning)	Portfolio Value (after 1 year)
ESG	QR 1,000,000	QR 2,016,609
Non-ESG	QR 1,000,000	QR 1,012,988

Discussion

- ESG stocks with low MSCI ratings (BB-C) show a positive correlation with high risk-adjusted returns excluding transactional costs, challenging prior research on ESG integration.
- ESG portfolio volatility was higher than the non-ESG portfolio. This could be due to under-diversification causing high idiosyncratic or systematic risk, as ESG portfolio selected stocks were from the riskiest sectors, compared to non-ESG portfolio.
- It could be interesting for SRI investors that ESG portfolio can outperform the benchmark using passive strategy, and motivate them towards ESG integrated investment.

Conclusion

- This study contributes to SRI/ESG literature in the GCC by empirically examining the impact of ESG inclusion on portfolio risk & return. ESG integrated portfolios show high risk and return, compared to non-ESG integrated portfolios.
- Qatar, an emerging market with a new ESG index, offers diversification opportunities, making this study valuable for responsible investors, but may be concerned for downside volatility.
- This study is limited to a specific time period, strategy, portfolio structure, and with ESG reporting challenges, suggesting future research on alternative investment strategies for SRI and institutional investors.

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