

Executive Summary

Is ESG the Succeeding Risk Factor in ASEAN Exchanges?

This study expands Fama-French three- and four-factor models with ESG factor, as well as apply a factor approach to measure the performance of ESG investment by constructing ESG pure factor portfolios and to test the validity of Fama-French five-factor model. Investigating the ASEAN Exchanges during September 2012 – June 2022, significant positive and negative effect of ESG related risk factors on stock returns. Classified by normalized ESG scores, ESG pure factor portfolios covers leaders, followers, loungers, laggards and unrated companies. Neither the leader nor the laggard have consistent outperformance risk-adjusted returns of both positive and negative, depending on ESG score providers. ESG factor based portfolios can generate significant alphas in either high or low sustainability risk groups. The findings are subject to ESG dimensions and ESG score providers. All in all, the evidence supports both mispricing scenario and risk factor scenario. Certain ESG attributes tend to be value relevant, but are not efficiently incorporated into stock prices. Although the evidence is not sufficient to consider ESG as an additional risk factor in the Fama-French model, ESG tilt in ESG pure factor portfolios can attribute to sustainability portfolio performance.