Tests of ESG-Screened BrandLoyalties' Portfolio Indexes

Objective

To determine the effect of ESG-screening on BrandLoyalties' portfolio indexes

Background

For many years BrandLoyalties, Inc. has had a group of published quantitative indexes for various mixes of US listed consumer equities. Their brand-popularity based investment strategy (called "Brand Luminosity" and peer reviewed in The Journal of Investing, June 2019) has produced outstanding and persistent returns for those indexes in back tests that start in 2008.

BrandLoyalties, Inc. began delivering "Brand Luminosity" metrics and signals to quantitative hedge fund clients ten years ago in 2012. In 2013 they started expanding their coverage to include non-US listed consumer equities, and they now feature coverage of over 5,300 globally listed consumer equities, with annual subscriptions available by geographic regions (U.S., Europe and Asia).

The metrics rank global consumer equities according to the growth rates of consumer interest in their respective brands. Their indexes started as simple proof-of-concept portfolios demonstrating the value of investing selectively in equities with the fastest growing brand popularity. The indexes are quantitatively reconstituted and rebalanced each quarter to include only equities currently within the best quartile of brand luminosity growth.

Adding ESG Screens to the Process

BrandLoyalties had been asked if they had tested ESG-screened versions of their broad and thematic indexed portfolios. To test this concept, they contacted me for new tests since I had performed the quantitative testing and co-authored the 2019 study.

The missing elements we needed to perform the study were ESG data and ratings for the universe of stocks covered by Rapid Ratings. To fill this gap, I requested a contribution of such data from IdealRatings, Inc. ("IdealRatings") for the companies covered by BrandLoyalties. IdealRatings is a web-based responsible investment data and solutions provider since 2006 that I had worked with in the past.

Methodology

Once IdealRatings kindly agreed to contribute their extensive time-series data, the methodology for testing became relatively straight forward:

(1) use IdealRatings data to build a master list of ESG qualified equites for each quarter;
(2) on a quarterly basis use BrandLoyalties' rankings to freshly assemble a portfolio containing only those equities with the fastest growing 'Brand Luminosity.'

(3) The resulting portfolios comprised equities with a IdealRatings ESG total score of 200 or higher, while the BrandLoyalties data was used to select each quarter's best 25% in terms of brand popularity growth.

The study was conducted using the IndexOne platform and combined historical data from both BrandLoyalties and IdealRatings for the 2008 through 2022 time period.

IndexOne is an index provider and performance calculation platform that is cloud-based. The company's site asserts that they provide the tools to build indices based on custom strategies that reflect clients' personal investment needs in addition to benchmarking and backtesting capabilities. BrandLoyalties is a client of IndexOne and was able to obtain permission for Quant Pioneers to assist in the backtests.

Results

The results included cumulative annualized returns of over 15.5% and a Sharpe Ratio of over 36.5. This constituted nearly 700 basis points of excess return relative to broad market indexes and more than 500 basis points relative to the most popular ESG exchange-traded fund.

A chart of the back tested results is below:
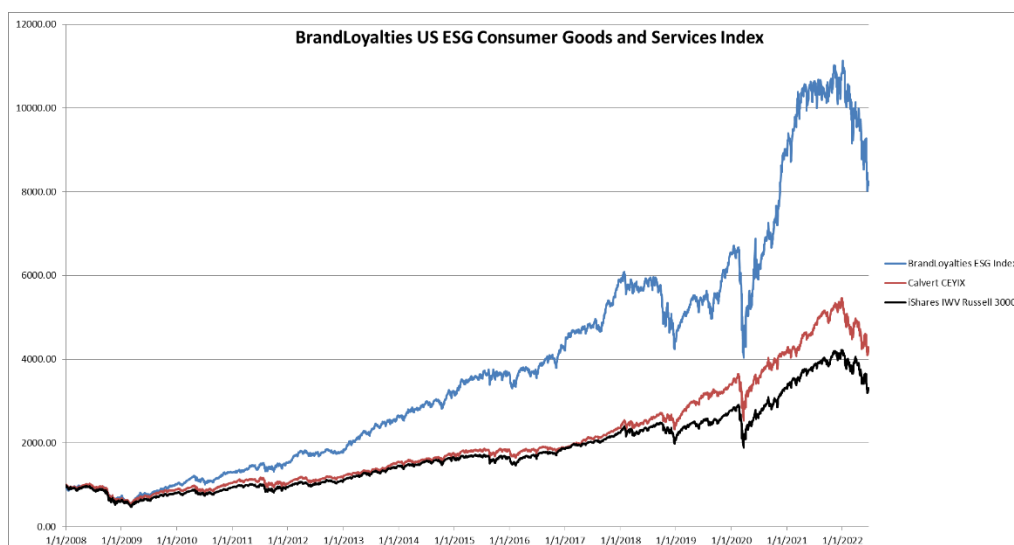
The excess returns and robust Sharpe ratios on the ESG sample were consistent with the published studies from 2019 using the entire US luminosity-score universe provided by BrandLoyalties. The ESG ratings used in the study were contributed by IdealRatings, a web-based supplier of responsible investment solutions since 2006.

Conclusion

Overall, the results for the ESG-screened consumer portfolios were very consistent with the outperformance posted before ESG screening. The testing has further validated the efficacy of BrandLoyalties' compliance-friendly data collection and ranking methodology in adding excess returns to nearly any imaginable collection of consumer equities.