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To open this issue, Xiong studies the impact of environmental, social, and governance (ESG) risk on US stocks through the lens of Sustainalytics' ESG risk-rating measure over the past decade. He reports that stocks with low ESG risk ratings (green stocks) not only have higher realized returns but also provide better tail-risk protection than stocks with high ESG risk ratings (brown stocks), especially during the COVID-19 crisis. Green funds and exchange-traded funds that hold green stocks have attracted significantly more fund flow than their counterparts, which is associated with the outperformance for both green funds and green stocks.

For the remainder of the issue, we focus on climate-related investing issues. First, Calandro, Hall, and Zheng profile the basic mechanics of natural catastrophe modeling and discuss how these mechanics are being influenced by climate change and the trend of recent natural catastrophe activity. The authors then discuss the complications of this output on insurance/financial services, the investment community, and policy advisors. Walkshäusl explores how a company's longer-term carbon emission growth rate—carbon momentum—affects future stock market and fundamental performance in international equity markets and finds that high carbon momentum has a negative impact on the company's future fundamental performance. He reports that carbon momentum holds unique information about the companies' carbon emission behavior that is independent from alternative measures, such as total emissions and emission intensity.

As we continue, Cheema-Fox, Realmuto LaPerla, Serafeim, Turkington, and Wang develop six strategies to decarbonize a portfolio for US and European-listed equities. After controlling for traditional factors, they find that the decarbonization factors that achieve greater carbon reduction also deliver greater alphas. Their results suggest that institutional flows could contain information about climate-related fundamentals. Next, Apostolou and Papaioannou provide a novel framework for understanding climate-related adaptation, mitigation, and transition risks and outline a method for valuing these risks in investors' portfolios. Their proposed setup serves as a call for action to long-term institutional investors to obtain accurate information on climate-related risks and develop appropriate frameworks for understanding these risks, regularly valuing them, and properly incorporating them into their investment decisions.

To conclude this issue, Bolliger and Cornilly propose a method to decompose the carbon intensity of a portfolio with respect to a benchmark into an allocation and a selection component. The carbon intensity decomposition allows for a better understanding of the sources of the difference between the carbon footprint of a portfolio and that of its benchmark. As such, it prevents greenwashing by analyzing whether the carbon exposure of a portfolio results from active stock selection choices on the part of the manager or passive sector exclusion decisions.

As always, we welcome your submissions. We value your comments and suggestions, so please email us at journals@investmentresearch.org.

TOPICS: *ESG Investing, exchange-traded funds and applications, manager selection, analysis of individual factors/risk premia**

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