

# DOING WELL WHILE DOING GOOD: THE CASE OF ISLAMIC AND SUSTAINABILITY EQUITY INVESTING

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## Keywords:

- Wavelet analysis
- Bayesian model averaging
- Efficient frontier
- Markov switching
- Sustainability investing
- Islamic equity



### Introduction

- Sustainable, responsible and impact investing (SRI) has witnessed significant growth and acceptance in the global financial industry in the last decade.
- Global SRI assets rose from \$13.3 trillion in 2012 to \$21.4 trillion in 2014.
- Islamic finance also progressed on a double-digit growth trajectory, increasing to \$1.8 trillion by 2013 (Kammer et al., 2015), but the growth has slowed to a single digit in last few years (Dar, 2017).
- Islamic equity funds represent 1/3 of Islamic funds worldwide.

#### Objectives of this study:

i. explore whether there is a cost attached to investing in a sustainable/ethical manner from the Islamic and/or sustainability perspectives.

ii. revisit the debate on the notion of “doing well while doing good” by examining the performance of two investment strategies: sustainable investing and Islamic investing.



### Data & methodology

#### Background on the DJ Sustainability and DJIS

DJ Sustainability*	DJIS**
<ul style="list-style-type: none"> <li>• Launched in 1999.</li> <li>• Includes 12 board market, 10 blue-chip, 3 specialty/screened, 8 diversified sustainability indexes.</li> </ul>	<ul style="list-style-type: none"> <li>• Launched in 2006.</li> <li>• The first global Islamic sustainability index.</li> <li>• Has higher average market capitalization (\$41.5 billion).</li> <li>• Technology (28.97%) and health care (20.56%) as dominant sectors.</li> </ul>

\*DJ Sustainability – Dow Jones Sustainability World Index  
 \*\*DJIS – Dow Jones Islamic Market Sustainability Index

#### Performance of sustainable and Islamic equities within the global asset classes portfolio

<p>This study examines the various aspects of four Dow Jones indexes:</p> <ul style="list-style-type: none"> <li>• Dow Jones Global Index (DJ Global)</li> <li>• Dow Jones Islamic Market World Index (DJ Islamic)</li> <li>• Dow Jones Sustainability World Index (DJ Sustainability)</li> <li>• Dow Jones Islamic Market Sustainability Index (DJIS)</li> </ul>	<ul style="list-style-type: none"> <li>• Dataset: from 1998 to 2013.</li> <li>• Data sources: Datastream and Bloomberg.</li> </ul>
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### Performance at different regimes: Markov switching analysis

Method	Goal
<ul style="list-style-type: none"><li>• Uses Markov switching method.</li></ul>	<ul style="list-style-type: none"><li>• To examine the performance of sustainable and Islamic equities within the global portfolio across different regimes (expansion and recession).</li></ul>

### Sector and factor exposures: Bayesian model averaging (BMA)

Method	Goal
<ul style="list-style-type: none"><li>• Uses Bayesian model averaging (BMA) approach.</li></ul>	<ul style="list-style-type: none"><li>• To measure the exposures of sustainability and Islamic equities to sector premiums (idiosyncratic risks) and factor premiums (systematic risks).</li><li>• To select the significant variables from the large candidate regressors.</li></ul>

### Diversification benefits in different investment horizons: Wavelet analysis

Method	Goal
<ul style="list-style-type: none"><li>• Applies Wavelet Coherence analysis.</li></ul>	<ul style="list-style-type: none"><li>• To identify the degree of diversification benefits of sustainable or Islamic equities across the presence of multiple horizons in investment (dynamic investors).</li></ul>

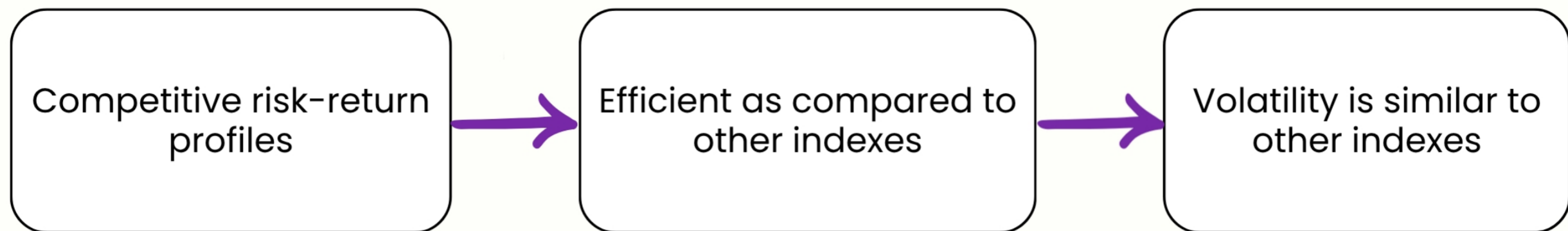
### Dynamic volatility: multivariate GARCH model and dynamic conditional correlations (DCC)

Method	Goal
<ul style="list-style-type: none"><li>• Applies MGARCH-DCC models.</li></ul>	<ul style="list-style-type: none"><li>• To understand how correlations and volatility change over time and when they are strong or weak in the financial markets.</li></ul>



## Conclusion

- This study demonstrates that Islamic sustainability equity investing offers:



- The findings:

Support the notion that is possible to do well while doing good.

Can be instrumental in strengthening the universality and acceptance of Islamic finance.



## Policy implications

This research suggests that:

**01** Islamic finance industry should proactively participate in mainstream sustainability investing.

**02** Islamic financial institutions should:

- i. consider adopt global recognized principles such as United Nations Principles for Responsible Investment (UN PRI) and corporate sustainability reporting.
- ii. participate in United Nations Environment Programme (UNEP) Financial Initiative.
- iii. strengthen their investment strategies and capacity in sustainable investing.
- iv. encourage clauses on responsible investment in Islamic fund management contracts.

**03** For portfolio managers: Islamic and Islamic sustainability stocks provide additional opportunity to diversify portfolio without sacrificing on the financial grounds.

## References

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