

The Relationship Between Firms' ESG And Stock Price Crash Risk

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Abstract

This study analyzes the impact of firms' ESG ratings on UK stock price crash risk using a Fixed Effects model. We utilized overall ESG ratings and individual ESG pillar scores, along with weekly stock prices of 140 firms in 6 FTSE All-Share sector indices from 2010 to 2022. The stock price crash risk was measured using Negative Conditional Skewness (NCSKEW). To assess the influence of the COVID-19 pandemic, we divided the sample into two periods: pre-COVID-19 (2010–February 2020) and during COVID-19 (March 2020–2022). This study contributes to UK literature by examining the impact of ESG ratings on stock price crashes, focusing on each ESG component rather than aggregate scores. It also highlights the evolution of these variables before and during COVID-19, aiding in understanding how economic crises affect these connections. The research fills a significant gap by studying the UK sectoral association, examining how each ESG component influences stock price stability and their potential for crisis hedging. The analysis was conducted in two sections: first, building a regression equation linking ESG ratings to stock price crash risk and evaluating their interaction during COVID-19; second, examining the sectoral link for a deeper understanding. Results indicated that the relationship between ESG ratings and stock price crash risk varies by component and sector. Notably, high social rating firms showed a stronger connection with stock crashes during COVID-19 compared to before the crisis. This research enhances financial economics and risk management understanding, emphasizing the strategic and policy importance of ESG in financial markets.

Keywords: covid-19, fixed-effect, sector, stability, finance