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Modified Piotroski Score for Higher Returns

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Abstract

The Piotroski score is a discrete number between 0-9 that determines the strength of a firm's financial position. It is a popular metric used to judge value stocks, with nine being the best and zero being the worst. Some of these criteria include Net Income, ROA, Long-Term Debt, Gross Margin, etc. In April 2000, Piotroski published the paper "Value Investing: The Use of Historical Financial Statement Information to Separate Winners from Losers," which demonstrated that the Piotroski score method would have seen a 23% annual return between 1976-1996 if the expected winners were bought, and expected losers shorted.

In this paper, we attempt to scrutinize the constituting parameters and apply our fundamental knowledge of economics to identify this method's shortcomings. Subsequently, we made suitable adjustments to the score to overcome these flaws and improve the overall portfolio returns. The constituting parameters are chosen in a way to achieve a better Sharpe ratio at a lower Beta.

Keywords: Piotroski Score, Sharpe Ratio, Value Investing.

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