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ESG and Impact: Finding a Way Forward

So-called ESG funds, which invest in firms which meet Environmental, Social, and Governance standards, now manage over 2.5 trillion dollars in global assets. Yet many critics argue that ESG funds have little or no positive impact on key issues such as climate change, and question the value of the ratings that drive them.

Groups on the political right have accused ESG funds of putting politics before their fiduciary responsibility to investors, and some states have passed or proposed anti-ESG legislation, including Texas and Florida. On the other end of the political spectrum, environmental groups have accused the ESG industry of greenwashing and being little more than a front for “business as usual.”

This Columbia University case study explores the debate around ESG. It draws from five interviews with industry leaders and key practitioners: Constance Hunter, Executive Vice President and Global Head of Strategy & ESG at AIG; Erin Leonard, Head of Sustainability at HSBC Asset Management; Caroline Flammer, Professor of International and Public Affairs and of Climate at Columbia University; Jon Hale, Global Head of Sustainable Investing Research at Morningstar; and Tariq Fancy, Founder of The Rumie Initiative and former Head of Sustainable Investing at BlackRock.

The case includes the following elements:

- Video Introduction and Discussions: Available online
- Written Case Study: This Document
- Annex A: Additional Images
- Annex B: Sample ESG Ratings Reports

What is ESG?

As the name suggests, ESG creates a framework for investing that focuses on environmental, social, and governance issues. ESG investments blend traditional investment information (e.g., capital, labor, intellectual property, markets, debt, equity, and other elements of the value chain) with a rigorous consideration of nonfinancial issues (e.g., the impact of carbon emissions, resource supply, or labor conditions).

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The big difference between ESG and conventional ways of evaluating risk is that ESG measures non-financial risk, while traditionally financial benchmarks are used to determine risk. A balance sheet shows financial performance, but an ESG report shows performance against nonfinancial goals, like carbon emissions or diversity and inclusion.

ESG is a useful tool that can be used in a variety of ways. An ESG performance evaluation can be used by asset managers to make decisions about ESG investments. It can also be used by a company to assess their own performance against ESG goals, and it can be used to assess the performance of clients.

Recently, ESG funds have been a centerpiece of great debate. An ESG fund is a pool of money that invests in firms which meet environmental, social and governance standards. At the end of 2022, ESG funds managed \$2.5 trillion in assets globally.¹ Europe was the largest market with over \$2 trillion in assets.² The United States was the second largest with over \$280 billion in ESG assets.³ In recent years, the interest in ESG funds has also exploded. In 2019, almost 500 actively managed funds in the US added ESG criteria to their prospectuses—up from less than 150 the year before.⁴

Today, ESG is everywhere—splattered across news headlines, on the agenda for global conferences, and the subject of business meetings. Since 2019, internet searches for ESG have increased by a factor of five.⁵ Over 90% of S&P 500 companies publish ESG reports, and the United States Securities and Exchange Commission (SEC) has considered mandating Climate Change Disclosures, explaining that “investor demand for...climate change risks, impacts, and opportunities has grown dramatically” in the last decade.^{6,7,8}

In a sense, ESG has already triumphed as an investment strategy. “Virtually every asset manager of any size or significance in the world today is using ESG to some degree in their investment process,” says Jon Hale, Global Head of Sustainable Investing Research at Morningstar Analytics, an investment data and research firm.

ESG’s Backstory

In the early ‘90s social and environmental factors started to be incorporated into socially responsible investing (SRI). In 1990, what was then called MSCI KLD, the prominent ratings agency that would lead to the formation of today’s MSCI, published the first SRI index. The Index was called the MSCI KLD 400 Social Index, and it allowed investors to consider social and environmental factors in their investment decisions.⁹

¹ Morningstar, *Sustainable Fund Flows: Q4 2022 in Review*, <https://www.morningstar.com/lp/global-esg-flows>

² Morningstar, *Sustainable Fund Flows: Q4 2022 in Review*, <https://www.morningstar.com/lp/global-esg-flows>

³ Morningstar, *Sustainable Fund Flows: Q4 2022 in Review*, <https://www.morningstar.com/lp/global-esg-flows>

⁴ Morningstar, “The Number of Funds Considering ESG Explodes in 2019,”

<https://www.morningstar.com/articles/973432/the-number-of-funds-considering-esg-explodes-in-2019>

⁵ McKinsey, *Does ESG Really Matter—And Why?*, <https://www.mckinsey.com/capabilities/sustainability/our-insights/does-esg-really-matter-and-why>

⁶ McKinsey, *Does ESG Really Matter—And Why?*, <https://www.mckinsey.com/capabilities/sustainability/our-insights/does-esg-really-matter-and-why>

⁷ SEC, *Public Input Welcomed on Climate Change Disclosures*, <https://www.sec.gov/news/public-statement/lee-climate-change-disclosures>

⁸ SEC, *SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors*, <https://www.sec.gov/news/press-release/2022-46>

⁹ MSCI, “Exploring 30 Years of ESG Indexes,” <https://www.msci.com/esg/30-years-of-esg>

The link between environmental and social factors and investing had been born, but it wasn't yet called ESG.

In 2004, a watershed U.N. report called *Who Cares Wins: Connecting Financial Markets to a Changing World* used the term ESG for the very first time, ushering in the new era of ESG. The report gave practical recommendations on how to integrate ESG into asset management and securities brokerage services, and was jointly released by the United Nations, the International Finance Corporation, and the Swiss Federal Department of Foreign Affairs.^{10,11}

This report also linked positive ESG performance with improved performance across several areas, including shareholder value, risk management, and reputation, demonstrating that environmental, social, and governance standards could be linked to performance outcome.¹² *Who Cares Wins* was endorsed by 20 financial institutions who collectively managed over \$6 trillion in assets, including HSBC, Goldman Sachs, Deutsche Bank, Morgan Stanley, and World Bank Group.

The creation of the 2004 *Who Cares Wins* report opened up an era of expansion of ESG funds and investments that has continued to this day.

ESG Vs. Impact Investing

But the ESG investment space has grown, so too has debate and confusion about ESG is, what it should be, and what it shouldn't be. One of the principal areas of contention is the connection that many people make between "ESG ratings" and "ESG Funds" – which are way of rating non-financial risk and of investing in firms that score well on these ratings, and "Impact Investing", which seeks to find and invest in firms who could potentially offer investors both financial and social returns.

While ESG and Impact investing are very different they are often connected in people's minds, and it is useful to review their differences.

During the process of creating an ESG evaluation, data from past performance is gathered and analyzed to assess how an organization performed on ESG metrics. This assessment is used to draw inferences about future risk and potential.

Impact investment is different. Instead of looking to past performance, impact investments look to the future with an eye towards making investments that will provide both financial and social returns. For social impact investing funds, yesterday's performance indicators matter less than tomorrow's potential. Investments in an emerging market, for example, often lack significant or reliable data on past performance of companies. Rather than relying on past-performance data like ESG, then, impact investors look for signs

¹⁰ International Finance Corporation, *Who Cares Wins – Connecting Financial Markets to a Changing World*, https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/publications_report_whocareswins_wci_1319579355342

¹¹ Forbes, "The Remarkable Rise Of ESG," <https://www.forbes.com/sites/georgkell/2018/07/11/the-remarkable-rise-of-esg/?sh=5ced96941695>

¹² International Finance Corporation, *Who Cares Wins – Connecting Financial Markets to a Changing World*, https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/publications_report_whocareswins_wci_1319579355342

about the future. In a sense, they enjoy greater latitude and are not held to the same level of fiduciary scrutiny.

Consider a wide range of differences between ESG and impact investment:

ESG	Impact Investing
Establishes a framework for investment, using past performance on key issues to signal a decision whether to invest.	Seeking to address public policy challenges as well as make a profit, impact investors look at future trendlines and analyses to make investments.
ESG investments, based on public standards and overseen by public bodies, must meet greater levels of fiduciary scrutiny.	By using public and social considerations to make smart as well as enlightened investment decisions, impact investors have little external scrutiny.
ESG is a risk-avoidance approach. By using past performance of companies to determine their commitment to ESG goals, the investor can make clear no/no-go decisions.	Impact investors are aggressively future-oriented. They seek to use forward-looking data and analysis to find investments. The hope is that socially responsible investing offers far greater opportunity for profitability than traditional bottom-line thinking.
ESG conforms with traditional investing in one important regard: it places finance and profit above over considerations. ESG offers a filter to sort investment opportunities but does not serve as a strategic driver of those decisions.	Impact investors seek to balance financial outcomes with social and environmental concerns.
Initiated and overseen by public bodies, ESG provides a framework for the policy goals of those bodies, industries, and other stakeholders.	Driven by private parties, impact investment stays focused on the needs of private actors by seeking to use public-oriented considerations to gain a market advantage.
Not all are ESG investments meet the goals of impact investments.	Impact-investments are all ESG-compliant

Source: Jaclyn Foroughi, "ESG Is Not Impact Investing and Impact Investing Is Not ESG," Stanford Social Innovation Review, November 2022.¹³

¹³ Stanford Social Innovation Review, *ESG Is Not Impact Investing and Impact Investing Is Not ESG*, https://ssir.org/articles/entry/esg_is_not_impact_investing_and_impact_investing_is_not_esg#

ESG at Three Leading Firms

The nuances of the various uses of ESG ratings are best illustrated in concrete cases. Below we explore how several leading firms use ESG ratings and criteria and tools in their investment process.

Morningstar – An ESG Ratings Agency

Morningstar is a Chicago-based global investment research firm founded by Joe Mansueto in 1984. In 2017, Morningstar acquired 40% of the premier ESG ratings and research agencies Sustainalytics.¹⁴ Sustainalytics, housed within Morningstar, runs a thriving ESG ratings practice that serves 18 of the top 20 asset managers and employs over 1,800 team members.¹⁵

Jonathan Hale, Morningstar’s Head of Sustainable Investing Research, joined the company in the mid 1990s as a mutual fund analyst, and worked on socially responsible investment (SRI) funds. As ESG became more important to investors in the 2010s, Hale became convinced that Morningstar should provide investors with ESG information that they could use to assess risk. Today, Hale runs the company’s leading ESG ratings system.

“Initially, the idea was to align investors with their values,” Hale explained, “If I move into the investment arena, I shouldn’t just leave my values at the doorstep.” Investors can make better investment decisions when they consider non-financial ESG data that do not show up in a financial analysis, Hale argues.

Hale explains that ESG ratings are complicated; over time, they become more refined with more voluminous and sophisticated data. A single ESG rating can be based on thousands of key performance indicators, known as KPIs. Some investors ignore the overall ESG score and instead “slice and dice” the individual KPIs to create a scorecard based on the indicators that are most important to them.

Creating an ESG rating would be impossible without massive data and sophisticated permutations of those data. “There are a lot of data providers in the ESG space today—dozens and dozens, maybe even close to a hundred,” Hale says. “There is just so much data out there [that] needs to be gathered, categorized, and assessed,” says Hale.

As ESG data continues to become more readily available, investors might be able to one day refresh an ESG report in real time, consuming ESG data on demand.

AIG – A Global Insurer Uses ESG to Mitigate Risk and Guide Sustainable Growth

While Morningstar provides an example of a leading ESG ratings firm, AIG provides an example of how a firm uses ESG ratings as part of its long-term growth and sustainability planning.

AIG is the world’s largest insurance firm. Headquartered in midtown Manhattan, the global insurance giant AIG shows how ESG can guide internal and external company operations. Founded in 1919 in

¹⁴ Morningstar, Press Release, “Morningstar and Sustainalytics Expand Their Sustainability Collaboration,” <https://newsroom.morningstar.com/newsroom/news-archive/press-release-details/2017/Morningstar-and-Sustainalytics-Expand-Their-Sustainability-Collaboration/default.aspx>.

¹⁵ Sustainalytics, “Who We Are,” <https://www.sustainalytics.com/about-us#facts>

Shanghai, China, AIG opened its first U.S. operation in New York in 1926.¹⁶ Today, AIG operates in 70 countries and jurisdictions.¹⁷

As the insurer of choice for many international financial companies, AIG acts as its clients' "silent" partner in many complex transactions — quietly participating in each transaction and adding the right safety nets in operations that range from issuance of debt, to creation of financial instruments, to international mergers and acquisitions and other international transactions.

AIG uses ESG in their own operations and to assess potential partners. Internally, AIG measures its own performance against specific ESG goals. Externally, AIG uses ESG to assess the risk of potential partners. Unlike investment groups, AIG does not offer ESG funds but instead uses ESG as a tool to conduct its own analysis.

Constance Hunter is the Executive Vice President and Global Head of Strategy & ESG at AIG. Before joining AIG in February of 2022, she served as Chief Economist for KPMG. Uniquely, Hunter's role combines business strategy with ESG analyses. Both strategy and ESG both play an "inextricably linked role in AIG's business model," she says.¹⁸

For Hunter, the "G" in ESG plays the pivotal role in evaluating potential partners. "If you're going to invest in a company, you want to make sure they have the right policies and procedures, checks and balances," she says.

With its focus on risk, the connection between ESG and insurance makes sense. ESG is a risk measurement tool; insurance is a risk-protection tool. The "S" in ESG—the social aspect—also plays an important role in risk mitigation in complex international transactions. "There are reams of data about how better decisions are made when you have more diverse perspectives," Hunter says. "Groupthink prevents people from seeing around corners or anticipating whether it's a positive future change that a company might want to take advantage of or whether it's a risk."

A company's ESG diversity rating can signal how likely a company is to bring a range of perspectives to the table.

HSBC

While AIG uses ESG to manage its operations, the global financial service company HSBC uses ESG ratings to create investment funds and inform investors of risks and opportunities. Founded in 1865 in Hong Kong to promote trade between Europe and Asia, HSBC now operates in 62 countries and territories around the world, employs 200,000 professionals, and manages more than \$2.9 trillion in assets.^{19,20,21}

¹⁶ AIG, "Our History," <https://www.aig.com/home/about/history>

¹⁷ AIG, "Our History," <https://www.aig.com/home/about/history>

¹⁸ AIG, *A Message from our Executive Vice President, Global Head of Strategy & ESG*, <https://www.aig.com/esgreports/home/a-message-from-our-evp-global-head-of-strategy-and-esg>

¹⁹ HSBC, "Our History," <https://www.hsbc.com/who-we-are/our-history>

²⁰ HSBC, "Creating Opportunities Together," <https://www.hsbc.com/who-we-are/our-people-and-communities>

²¹ HSBC 2022 DataPack available for download at "Annual Results 2022," <https://www.hsbc.com/investors/results-and-announcements/all-reporting/annual-results-2022-quick-read>

HSCB launched its first ESG fund 20 years ago and has been building its ESG practice steadily ever since.²² In 2021, HSBC reported 826 sustainable finance products, including green bonds, sustainability bonds, social loans, green trade loans, sustainable trade instrument, and many others.²³ HSBC has been publicly recognized as a leader in sustainable finance. In 2020, Euromoney named HSBC World's Best Bank for Sustainable Finance.²⁴

Erin Leonard, the Head of Sustainability for HSBC Asset Management, oversees the management of \$600 billion in assets globally.²⁵ For Leonard, ESG is about seeing an investment from both sides—both risks and opportunities. HSBC uses ESG ratings to find hidden values and risks, and it uses ESG funds to actively promote social and environmental change.

“As stewards of our investors’ money, we need to take into account all risks and we want to consider all opportunities,” she says. “In either context, sustainability is relevant. Our fiduciary responsibility to our clients is about managing risk, but it's also about identifying emerging opportunities in the transition economy.”

In addition to overseeing ESG funds and initiatives, Leonard’s portfolio also includes impact investments. In 2020, for example, HSBC partnered with the climate change investment firm Pollination Group to form Climate Asset Management, an asset-management company focused on natural capital. Leonard recognizes that having both ESG and social impact products in the same business unit can be confusing to investors.

However broad and sweeping its agenda, Leonard recognizes that ESG focuses primarily on mitigating risk. Leonard warns against conflating two distinct goals: “Many people think they're putting their money towards something that's going to make things better, rather than putting their money towards something that's just avoiding climate risk.”

Still, risk mitigation can provide a strong platform for more aggressive efforts to pursue ESG goals. HSBC’s multipronged approach to ESG has become a major strength and allows HSBC to mitigate risk as well as seek out opportunity across environmental, social, and governance standards.

The Debate Over ESG

As ESG-connected funds and investments have grown, so too has criticism of the sector, from both the left and right ends of the political spectrum.

One of ESG most visible critics is Tariq Fancy, former Head of Sustainable Investing at BlackRock, who argues that ESG funds have little or no positive impact on the key issues they claim to champion, like climate change. “ESG has been presented as a magical win-win for investing,” says Fancy. “But the problem is that the mechanics underneath most of it don't really add up.”

²² Erin Leonard interview with Adam Stepan.

²³ HSBC, 2021 Datapack, <https://www.hsbc.com/who-we-are/esg-and-responsible-business>

²⁴ Euromoney, “World’s Best Bank for Sustainable Finance 2020: HSBC,” <https://www.euromoney.com/article/27g0tbzca93zph51zgjv8/awards/awards-for-excellence/worlds-best-bank-for-sustainable-finance-2020-hsbc>

²⁵ Erin Leonard interview with Adam Stepan.

Tariq Fancy made a name for himself after publishing *The Secret Diary of a 'Sustainable Investor,'* a scathing four-part essay series that critiques sustainable investing.²⁶ Shortly after that work's release, he delivered a 2022 TEDx Talk entitled "I've Seen the Worst of Capitalism—Here's How We Fix It."²⁷ Fancy has voiced his controversial opinions on CNBC, Yahoo Finance, and other outlets. When he isn't talking about ESG, he runs The Rumie Initiative, the education technology nonprofit that he founded in 2013.²⁸

In *The Secret Diary*, Fancy charges that ESG often morphs into marketing. ESG, he says, poses a dangerous distraction from necessary government regulation tools, like a carbon tax, that could advance environmental, social, and governance goals. ESG, he said, is free-market capitalism dressed up as making the world a better place. It makes you feel good about *not* changing the system, in his view.

"It's like giving wheat grass to a cancer patient," he says. "Eventually you realize the patient is delaying chemotherapy."

Fancy began his career in investment banking working on distressed investments. In 2018 he became the first global Chief Investment Officer for Sustainable Investing at BlackRock, where he was responsible for integrating ESG into its investment processes. That year, BlackRock CEO Larry Fink shocked the financial world with his announcement of a new focus on socially conscious investing.

"I thought it was interesting," Fancy said, "There were areas I wasn't sure about, but it looked like we could use the gears of capitalism to create an impact at scale."

But Fancy quickly became disillusioned. As he spoke at sustainable investment events in London, New York City, and Geneva, he began to question the premise that industry could address climate change and other complex issues without government action. Most people working on ESG investing at BlackRock came from do-good, philanthropy backgrounds. As a result, Fancy lamented, they didn't understand how investments work.

Fiduciary scrutiny, Fancy argues, often sidelines ESG goals in favor of an investor's legal obligation to prioritize financial returns.

"As long as something is legal and makes money, someone will find a way to invest and exploit it," Fancy says. "That's not a bug in capitalism—that's a feature. That's exactly how the system is supposed to work. Otherwise, it's not an efficient system. So, there are government tools we need to use to manage the system."

ESG, Fancy argues, has not significantly impacted problems like carbon emissions or inequality, even though the number of ESG funds has exploded in recent years.

²⁶ Medium, *The Secret Diary of a 'Sustainable Investor,'* <https://medium.com/@sosofancy/the-secret-diary-of-a-sustainable-investor-part-4-epilogue-f18304fd9db7>

²⁷ TedxToronto, "I've seen the worst of capitalism - here's how we fix it," <https://www.youtube.com/watch?v=NZxKsvS0AH4>

²⁸ The Rumie Initiative, <https://about.rumie.org/>

A Systems-Level Approach

The School of International and Public Affairs at Columbia University recently launched the Sustainable Investing Research Initiative (SIRI), led by ESG and impacting investing expert Professor Caroline Flammer.²⁹ Its mission is to foster cross-disciplinary scholarship, education, and dialogue on the interplay and interdependencies between investment and the most complex challenges facing our world.

In absence of effective public governance, private and public sectors are increasingly incorporating ESG considerations into their investment practices to help finance and promote a more sustainable world. Yet, as Flammer points out, “key impediments remain in efforts to mitigate climate change, preserve biodiversity, reduce poverty and social inequalities, and address other grand societal challenges”.

For Flammer, critical factors are needed to address these challenges. In particular, she says, “these factors include i) the adoption of a system-focused approach, taking into account how business and investment practices impact the broader (environmental, social, and economic) system and, vice versa, how the system impacts business and investment practices; ii) the development of better measures to track progress toward the mitigation of system-level challenges; and iii) the creation of public-private partnerships to fill the financing gap, using development funding to increase private sector investments in addressing these challenges.”

Missing Pieces: Regulation, Partnerships, or Something Else?

For many involved in the debates around ESG, one of the crucial questions is “what is the role of government in addressing societal issues, and what is the role of private actors?”

Tariq Fancy attacks the idea that major problems can be solved without government regulation. ESG deserves credit at least for identifying key challenges and metric, he says, but only government action can take the issue beyond rhetoric. Regulations could address two big criticisms of ESG: there are no agreed-upon universal standards for ESG metrics, and all reporting is voluntary.

“We have to dispense of the fallacy that government regulation is anti-capitalist,” he said. “That’s like saying referees who call fouls are anti-basketball.” All major policy debates, he adds, turn on a simple question: “Are we relying on mandatory or voluntary compliance?” Without mandates, he says, free riders will undermine collective action.

Jon Hale of Morningstar is optimistic about the state of ESG reporting, in part because its reliance on voluntary reporting has gone down in recent years. “There is a lot of information being collected by ESG data providers that’s not coming from companies,” he says, and this information is being used in ESG ratings.

For many observers, the solution lies in a combined approach. For many, the success of global efforts to produce a COVID vaccine offers a model for the sort of public-private collaboration on complex, systems-level, dynamic problems that is needed.

²⁹ SIRI, <https://www.sipa.columbia.edu/global-research-impact/initiatives/sustainable-investing-research-initiative-siri>

“We look at the pandemic as a sort of policy playbook,” says Constance Hunter of AIG. “We used public-private partnerships to harness the research and development capacity of private businesses. We put out the proper incentives. We said that if you develop this, we promise we will buy it from you.”

Such partnerships could also be useful in reducing carbon emissions. An international carbon market, akin to the carbon market under the Kyoto Protocol from 2008 to 2012, could combine the efficiency of the private sector with the power of government regulation.³⁰

With carbon credits, private capital could enter emerging markets while advancing the environmental goals of ESG. “Carbon credits are a way of facilitating funding for projects in emerging markets,” says Erin Leonard of HSBC. “We’re seeing some of the cash-rich corporates looking to invest in renewable energy or forestry and agriculture as a way to green their supply chains.”

Does ESG Mix Apples and Oranges?

Beyond the question of the role of government vs. the role of private actors, perhaps the biggest ongoing question in ESG debates, is whether the “E” of Environment, the “S” of Social and “G” of Governance should be grouped together at all.

Constance Hunter “firmly stands in the no camp,” she says. Investors look at these three factors separately when making decisions. “The majority of players in the field don’t aggregate them.”

Tariq Fancy agrees. “No investor would ever take a bunch of random indicators, on things like emissions, wastewater, gender policies, and other unrelated issues and mash them into one single score,” he says. “It just doesn’t make investment sense.”

So what is the best way to relate these three worlds? Governance has long been considered a crucial part of investment decisions, Fancy notes. Environmental issues often require regulation. But social issues vary widely in their importance and complexity.

“There’s a whole basket of issues in the ‘S’ bucket around gender ideology and other social causes that are important to society but not easy to regulate,” Fancy says. “From a movement perspective, we could get ten times more done by focusing on these issues separately. There is a viewpoint among a lot of senior business leaders that they’re getting pushed into social positions they don’t necessarily agree with and that the left’s method of creating change is public shaming and forcibly imposing values.”

From a Texas Showdown to a National Fight

Social issues drive the most contentious ideological debates in the world of responsible investing. Conservatives see ESG as an illicit effort to impose a liberal ideology on business. Republican-controlled legislatures of Texas and Florida in 2022 banned state investments in ESG funds. Overall, 24 states have taken legal action against ESG or are considering doing so.³¹ In 2022, 176 ESG-related bills were introduced

³⁰ UNFCCC, “What is the Kyoto Protocol?”, https://unfccc.int/kyoto_protocol

³¹ Consumer’s Research, “Anti-ESG Actions and Legislative Tracker,” <https://consumersresearch.org/esg-actions/#states>

and 23 were ultimately enacted into law.³² Texas had the highest number of anti-ESG bills of any state. By the spring of 2023, 230 ESG-related bills were introduced in state legislatures.³³

In 2023 Florida Governor Ron DeSantis made fighting “woke” ideology (including ESG) part of his political platform. DeSantis called ESG as “an attempt to impose ruling class ideology on society through publicly traded companies and asset management.” ESG, he said, “provides a pretext for CEOs to use shareholder assets to target issues like reducing the use of fossil fuels and restricting Second Amendment rights.”³⁴

ESG has become a bogeyman on Fox News and other right-wing outlets. Consider this Fox headline: “ESG Proponents Are Corporate America's 'Self-Appointed Thought and Governance Police'.”³⁵ The website Liberty Nation also emphasizes culture wars in its coverage: “ESG Investing: The Destroyer of Economies – and Democracies?”³⁶ Elon Musk, the controversial owner of Twitter, joined the attack: “ESG is a scam. It has been weaponized by phony social justice warriors.”³⁷

Environmentalists often warn against “virtue signaling” and “greenwashing” in corporate engagement on environmental issues. Absent clear and effective regulation, they say, corporate involvement in ESG is just a form of public relations.

“Greenwashing sins will never disappear, since it is human nature to exaggerate the good and downplay the bad,” notes columnist Eric Reguly of the Toronto *Globe and Mail*. “But as ESG investing moves into the mainstream for the sake of the planet, the most deceitful claims will become easier to catch. Governments can only do so much to prevent runaway global warming. If investors use credible ESG ratings to ensure that companies become cleaner, everyone wins.”

Some argue that even if the government fails to take direct action on issues like climate change, it can at least still police corporate claims. The Securities and Exchange Commission in 2022 published new rules to standardize ESG disclosures to prevent false claims about company actions. The SEC fined BNY Mellon Investment Adviser \$1.5 million for making false statements about its ESG funds.³⁸

The Future of Investing?

Whatever the pros and cons of ESG, simple demographics suggest that it could represent the future of investing.

³² Consumer’s Research, “Anti-ESG Actions and Legislative Tracker,” <https://consumersresearch.org/esg-actions/#states>

³³ Consumer’s Research, “Anti-ESG Actions and Legislative Tracker,” <https://consumersresearch.org/esg-actions/#states>

³⁴ Ron DeSantis, *The Courage to Be Free Florida’s Blueprint for America’s Revival* (HarperCollins, 2023).

³⁵ Fox News, Laura Ingraham: ESG proponents are corporate America’s ‘self-appointed thought and governance police,’ <https://www.washingtonexaminer.com/restoring-america/courage-strength-optimism/esg-investments-failures-show-states-right-fight-green-investing-agenda>

³⁶ Liberty Nation, *ESG Investing: The Destroyer of Economies – and Democracies?*, <https://www.libertynation.com/?s=ESG>

³⁷ Twitter, Elon Musk, <https://twitter.com/elonmusk/status/1526958110023245829>

³⁸ Kate Davidson and Aubree Eliza Weaver, “A Sustainable Crackdown,” *Politico*, May 25, 2022.

As the ESG market continues to grow, ESG funds have become more popular among women and young investors.³⁹ One survey found that 79% of women and young investors with a minimum investable asset of \$100,000 were interested in sustainable investing.⁴⁰ They see ESG playing a growing role in the global economy as investors and consumers alike focus more intently on a zero-carbon future.

AIG has committed to using rigorous ESG metrics in its global operations to both improve its competitiveness and contribute to important policy goals. “We have committed to be net zero in our underwriting and our investments by 2050 or sooner,” Constance Hunter says. “We want to make sure we can do it first before asking our clients.”

“ESG is not something that is parked off to the side and cornered off from the rest of the company,” Hunter says, “In fact, it’s front and center.” Erin Leonard adds: “ESG brought social and climate risks into focus on the world stage.”

ESG will evolve in tandem with climate change, energy independence, modern farming, water issues, and social justice issues. “We’re on a journey,” Constance Hunter says. “In fact, we’re just getting started, but we can’t let that fact hinder our progress.”

ESG critic Tariq Fancy hopes that journey includes recalibrating both ESG’s focus and its method. “The ESG space is going to need to reform and become better at what it does in theory, but not practice,” he said. It is also crucial that people accept that the private sector cannot do this all alone. “We should accept the limitations of what the ESG industry and the financial services industry can do without regulation to level the playing field” Fancy argues.

For Morningstar’s Jonathan Hale, the private sector will make a major impact on these challenges—and is motivated to do so.

“ESG is here to stay because companies realize that addressing their basic sustainability challenges is good for their bottom line,” he says. “It’s a better way to do business, and no one wants to be an ESG laggard. We’re in what I think of a paradigm shift away from shareholder primacy to one that some people call shareholder capitalism.”

³⁹ Morningstar, *10 Reasons Why ESG Won’t Be Stopped*, <https://www.morningstar.com/articles/1123647/10-reasons-why-esg-wont-be-stopped>

⁴⁰ Morningstar, *10 Reasons Why ESG Won’t Be Stopped*, <https://www.morningstar.com/articles/1123647/10-reasons-why-esg-wont-be-stopped>

Annex A – Original Documents

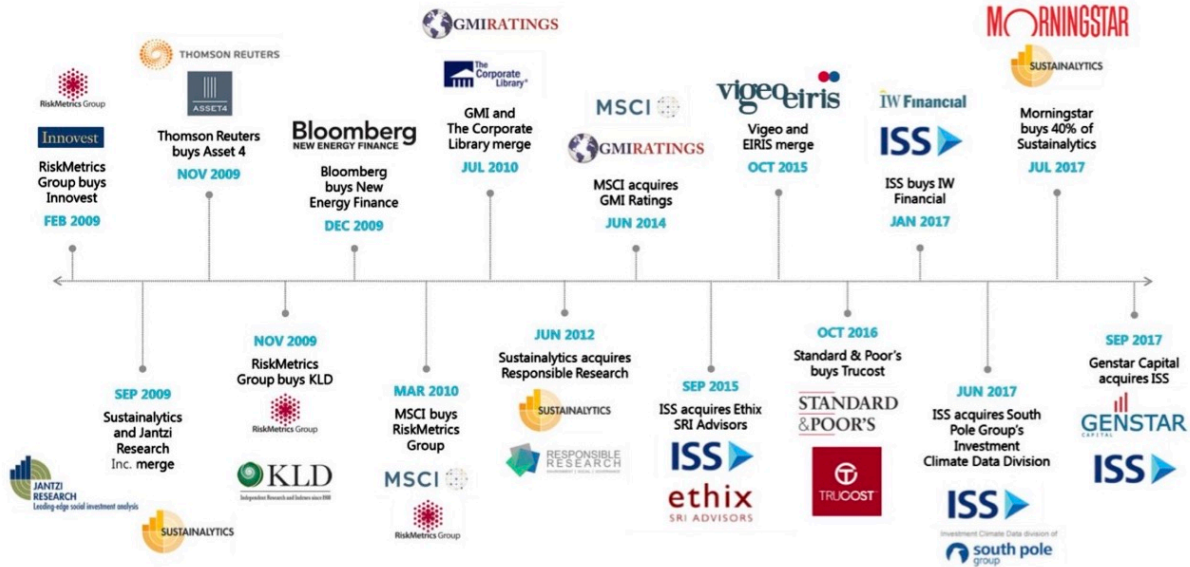


Figure 1: ESG data vendor consolidation⁴¹

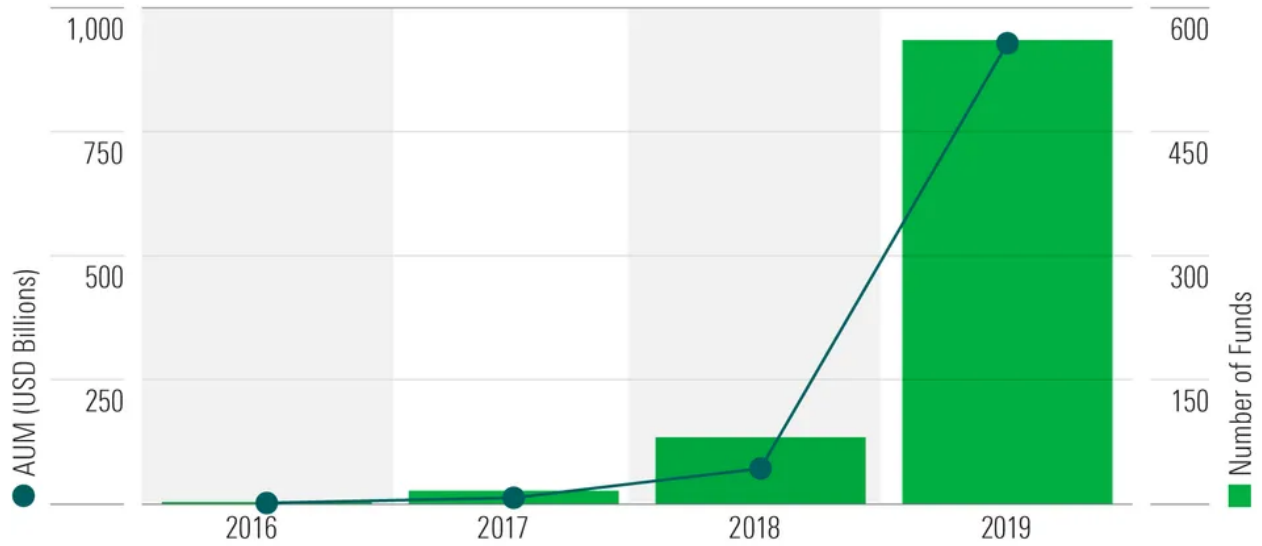
⁴¹ Figure from Brown Flynn (2018): The ESG Ecosystem Understanding the Dynamics of the Sustainability Ratings & Rankings Landscape, p. 6. Retrieved from “Exploring Social Origins in the Construction of ESG Measures” working paper, Saïd Business School, University of Oxford, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3212685.

Dimension	Sustainalytics	Morning star	EIRIS	Vigeo	MSCI	KLD	Oekom	ISS	GES Internat.
Geography (HQ)	NL (Amsterd.)	US (Chicago)	UK (London)	France (Paris)	US (NYC)	US (Boston)	Germany (Munich)	UK (London)	Sweden (Stockholm)
Establishment	Merger of Jantzi Research (Canada), DSR (NL), Scoris DE and AIS (Spain).	Joe Mansueto creates start-up to provide private investment research.	Research Entity of EIRIS Foundation for churches and charities.	Created by N. Notat, president of French labour union	Founded by Morgan Stanley to take over indexing business of Capital Internat.	Created as social investment research business by Kinder, Lydenberg, & Domini.	IPO of Ökom GmbH, a German environmental ranking company	Started by Bob Monks to create more active voting behaviour	M. Furugård and Nyman, activists/economists, create CSR consulting firm Caring Capitalism.
Year	1992 (Jantzi)	1984	1983	2002	1986	1988	1993	1985	1992
Key Moment	2009: Creation of Sustainalytics	2010: 40% Acquisition of Sustainalytics	2005: Vigeo and Eiris merge into Vigeo-EIRIS		2010: Acquisition of KLD and creation of MSCI ESG Research		2018: Acquisition of Oekom and creation of ISS-oekom		2003: Branded as GES.
Company structure	Private shared capital.	Publicly traded on NASDAQ	Private: investors (62%), NGOs/ unions (24%) companies (14%)		Publicly listed on NYSE		Privately held by Genstar Capital		Private Limited Company.
Early business	Sustainability performance research	"Informing and empowering private investors"	Investment research for NGOs and churches.	Monitoring for investors and CSR Audits.	Pioneering the market for global equity indexes.	Performance benchmarks and RI research	Environmental rating.	Raise proxy voting of institut, investors.	CSR Consulting
Current business	ESG Data, Analytics and Services	Financial rating, asset management etc.	ESG Data and Analytics & Company Auditing		Financial rating, asset management etc.	ESG Data, Analytics and Services	Proxy Voting, ESG Data, Analytics and Services		Engagement Services

Figure 2: Corporate history and establishment of select ESG data vendors.⁴²

⁴² "Exploring Social Origins in the Construction of ESG Measures" working paper, Saïd Business School, University of Oxford, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3212685. The authors of this working paper pooled this information from publicly available sources—corporate websites, corporate reports, and other public company sources.

The Number of ESG Consideration Funds Exploded in 2019



Source: Morningstar (author). Data as of 12/2019.

Figure 3: The number of funds considering ESG exploded in 2019—jumping from less than 150 in 2018 to nearly 600 the following year.⁴³

⁴³ Morningstar, “The Number of Funds Considering ESG Explodes in 2019,” <https://www.morningstar.com/articles/973432/the-number-of-funds-considering-esg-explodes-in-2019>

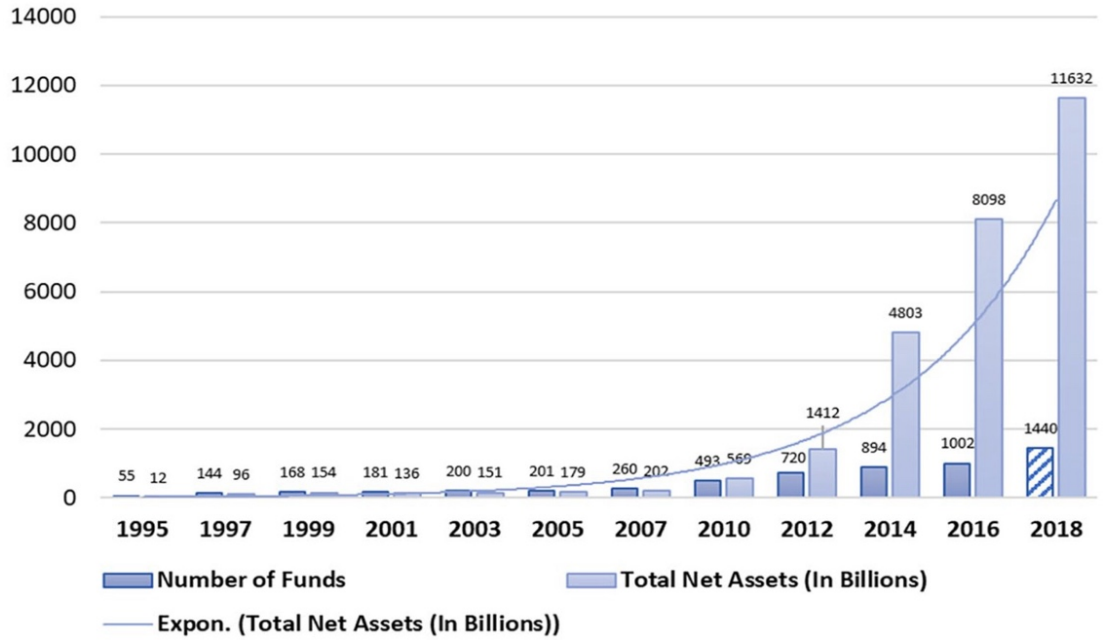


Figure 4: Growth of investment funds using ESG data since 1995.⁴⁴

⁴⁴ “The Social Origins of ESG: An Analysis of Innovest and KLD,” https://teacherscollege.primo.exlibrisgroup.com/discovery/search?query=any,contains,The%20Social%20Origins%20of%20ESG:%20An%20Analysis%20of%20Innovest%20and%20KLD&tab=Everything&search_scope=MyInst_and_CI&vid=01TCCU_INST:01TCCU&lang=en&offset=0

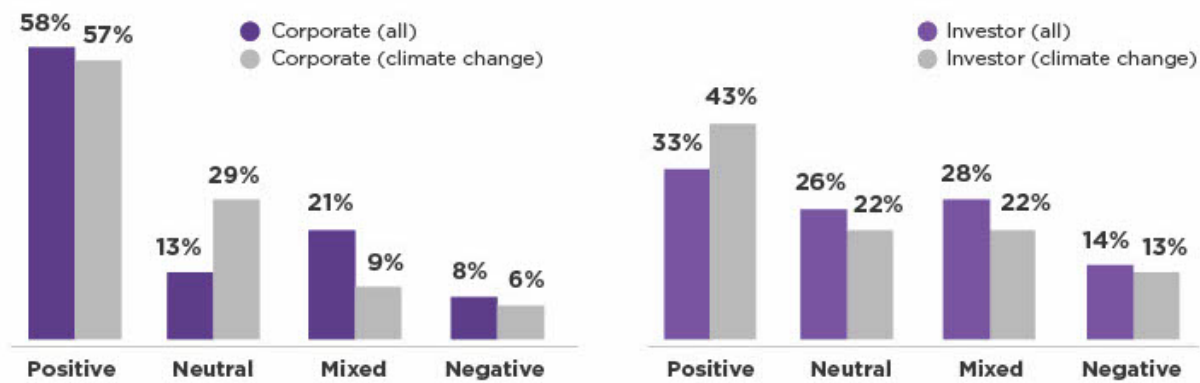


Figure 5: In a review of 1,000 research papers from 2015 – 2020, NYU Stern Center for Sustainable Business and Rockefeller Asset Management found an overall positive relationship between ESG and financial performance. Very few studies found a negative correlation between ESG and financial performance (based on 245 studies published between 2016 and 2020).⁴⁵

⁴⁵ New York University Stern, Center for Sustainable Business, *ESG and Financial Performance: Uncovering the Relationship by Aggregating Evidence from 1,000 Plus Studies Published between 2015 – 2020*, <https://www.stern.nyu.edu/experience-stern/about/departments-centers-initiatives/centers-of-research/center-sustainable-business/research/research-initiatives/esg-and-financial-performance>

HSBC
HSBC Holdings plc
Sustainable Finance - Summary

Capital Markets/Advisory ¹	331	48.7	189	30.0	520	78.7
Balance Sheet Related Transactions - Total ¹	427	26.2	178	10.4	605	36.6
Lending Transactions ²	366	25.5	169	10.2	535	35.7
Guarantee Transactions ²	36	0.5	2	0.1	38	0.6
Liabilities Transactions ² (deposits/issuances)	25	0.2	7	0.1	32	0.3
Investments (Assets under Management - net new flows) ³	68	7.7	29	3.7	68	11.4
Total Contribution	826	82.6	396	44.1	1,193	126.7

Sustainable Finance - Product View

	2021		2020		Cumulative	
	Volume	\$bn	Volume	\$bn	Volume	\$bn
Green Bonds	152	20.0	104	9.9	256	29.9
Social Bonds	38	11.1	29	9.7	67	20.8
Sustainability Bonds	69	11.2	44	8.2	113	19.4
Transition Bonds	4	0.2	1	0.1	5	0.3
Sustainability Linked Bonds	52	5.0	5	1.1	57	6.1
Short Term Debt	8	0.2	1	0.1	9	0.3
Green Loan	81	4.0	42	2.1	123	6.1
Other Green Qualified Lending	91	1.5	56	2.6	147	4.1
Social Loans	0	0.0	0	0.0	0	0.0
Social Qualified Lending	3	0.2	0	0.0	3	0.2
Sustainability Linked Loans	164	18.2	33	2.3	197	20.5
Green Trade Loan	21	0.2	5	0.1	26	0.3
Sustainable Trade Instrument	36	0.5	2	0.1	38	0.6
Sustainable Supply Chain Finance	3	1.2	0	0.0	3	1.2
Sustainable Finance	722	73.5	322	36.3	1,044	109.8
DCM	0	0.0	0	0.0	0	0.0
ECM	8	1.0	4	0.3	12	1.3
Finance Advisory	0	0.0	1	0.6	1	0.6
Project Finance	3	0.2	33	3.1	36	3.3
Sustainable Infrastructure	11	1.2	38	4.0	49	5.2
Investments - ESG Assessed ³	59	6.4	23	0.7	59	7.1
Investments - Thematic ³	7	1.0	5	2.6	7	3.6
Investments - Impact ³	2	0.3	1	0.4	2	0.7
Green Deposits	3	0.2	0	0.0	3	0.2
Structured Green Bonds	22	0.0	7	0.1	29	0.1
Sustainable Investment	93	7.9	36	3.8	100	11.7
Total Contribution	826	82.6	396	44.1	1,193	126.7

 Figure 6: HSBC Sustainable Finance Data, 2021⁴⁶
⁴⁶ HSBC ESG Datapack 2021, <https://www.hsbc.com/who-we-are/esg-and-responsible-business/esg-reporting-centre>

Annex B – Sample ESG Ratings Reports

Sustainalytics ESG Risk Rating Summary Report: <https://connect.sustainalytics.com/esg-risk-rating-sample-report>

S&P ESG Evaluation for National Grid PLC: <https://www.spglobal.com/ratings/en/research/pdf-articles/220929-esg-evaluation-national-grid-plc-101567022>

MSCI ESG Ratings Brochure: <https://www.msci.com/documents/1296102/21901542/MSCI+ESG+Ratings+Brochure-cbr-en.pdf>