

# The Origins and Consequences of the ESG Moniker

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*Discussion of the paper*  
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# Outline

1 **Brief summary**

2 **Suggestions**

The paper studies the **ESG** moniker.

- Where does term ESG **come from**? → History
- What is the term ESG **used for**? → Usage
- What is the term ESG **misused for**? → Critique

## What were the key moments in the history of the term ESG?

- **1999:** A speech by Kofi Annan (then-Secretary General of the UN) at the **Davos WEF** in which he proposed a “Global Compact,” directly urging business leaders to join the UN in promoting principles that would provide a foundation for a sustainable global economy.
  - **2004:** Kofi Annan wrote to the CEOs of 55 of the world’s leading financing institutions inviting them to join in a [new] initiative, under the auspices of the Global Compact, titled “**Who Cares Wins.**”
- Out of this initiative came a report using the new term “**ESG**”.

## Why does it matter?

Because **trillions of dollars** are already invested according to ESG principles:

- According to the ESMA report from March 24, 2022: “Out of a sample of 27,000 EU funds representing **EUR 10 trillion** assets under management, **30%** included in their precontractual documentation an SFDR Article 8 or Article 9 statement.”

Because it turns out that ESG means **different things to different people...**

- Therefore, this is a very important paper!

# Outline

1 **Brief summary**

2 **Suggestions**

# Suggestion #1

# What does it mean to be sustainable?

One example field in which this term has a straightforward meaning is **fishery**:

“A conventional idea of a sustainable fishery is that it is one that is harvested at a sustainable rate, where the **fish population does not decline over time because of fishing practices.**”





# What is ESG in the context of finance?

## Suggestion #1: Expand the section on ESG with the definition from the European Commission

- Until recently, there was no official definition.
- But the European regulator recognized that a common language and a clear definition of **what is “sustainable”** is needed and came up with a common classification system for sustainable economic activities, or an **“EU taxonomy.”**

# What is ESG in the context of finance?

## Suggestion #1: Expand the section on ESG with the definition from the European Commission

“Sustainable finance refers to the process of taking **environmental, social and governance (ESG) considerations into account** when making investment decisions in the financial sector, leading to more long-term investments in **sustainable economic activities and projects.**”

Source: European Commission

## Suggestion #2

## **Suggestion #2: When relating the term ESG to CSR, I noticed one additional difference that is currently not mentioned in the paper**

What is corporate social responsibility (CSR)? Again, let us rely on its EU's definition:

“CSR is the responsibility of enterprises for their impact on society and, therefore, it should be company led. Companies can become socially responsible by:

- integrating social, environmental, ethical, consumer, and human rights concerns into their business strategy and operations
- following the law.”

Source: European Commission

**Suggestion #2: When relating the term ESG to CSR, I noticed one additional difference that is currently not mentioned in the paper**

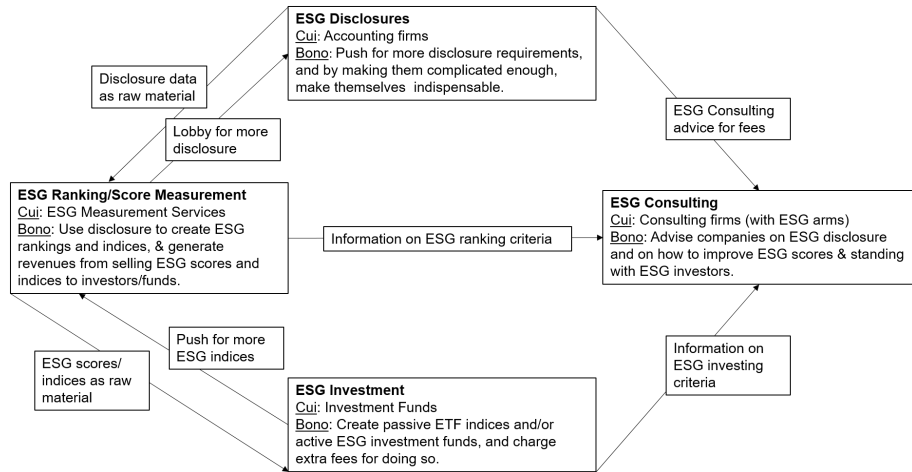
Is ESG a better term than CSR?

- One could argue so.
- Why? Because “**CSR**” says that “we need to be as responsible as society **currently** expects us to be”.
- But “**ESG**” says that we need to prepare ourselves for the major **future** challenges.

## Suggestion #3

# ESG is for many players a major business opportunity

## Suggestion #3: Talk about the “business case for ESG” in the asset management industry



Source: Figure by Aswath Damodaran

## Suggestion #4



# ESG investing and the use of the flexibility embedded in this umbrella term

## Suggestion #4a: Talk about how subtle wording differences can lead to funds invested quite differently

- **ESG Integrated** – ESG analysis may inform how we evaluate companies and issuers
- **ESG Aligned** – ESG criteria are used to screen out companies and issuers
- **ESG Enhanced** – ESG analysis informs how we evaluate companies, the universe of eligible securities, and our portfolio construction process
- **ESG Impact** – Capital is invested to seek to benefit from or accelerate specific ESG trends
- **ESG Catalyst** – Strategies that seek to advance diversity among capital market participants

Source: Goldman Sachs Asset Management 2021

Many funds are merely ESG Aligned while some newcomers might believe that they are ESG Impact or even Catalyst.

# ESG investing and the use of the flexibility embedded in this umbrella term

## Suggestion #4b: Amend the statement on the cost-effectiveness of some ESG funds

### Many ESG Funds Are Just Expensive S&P 500 Indexers

Bloomberg OPINION

Aaron Brown

Published On 04:30 PM IST, 07 May 2021

Last Updated On 05:15 PM IST, 10 May 2021

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Source: Bloomberg Opinion

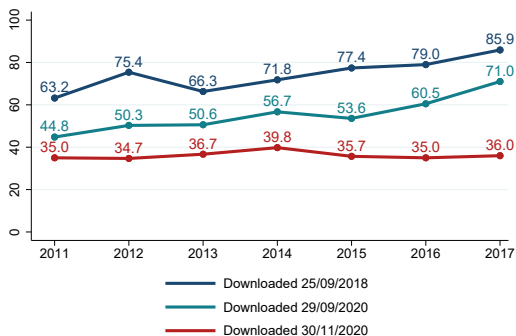
- **Vanguard S&P 500 ESG ETF** had an expense ratio of **0.12%** (now only 0.09% since 12/17/2021).
- **Vanguard S&P 500 ETF** has an expense ratio of **0.03%**.  
→ One might be paying multiple times more for almost perfect tracking...

## Suggestion #5

# ESG and its link to financial performance

**Suggestion #5: With Florian Berg and Zacharias Sautner we show that the positive relationship between ESG ratings and returns might have been **retroactively introduced into the database** by one of the major ESG ratings providers.**

- Therefore, depending on when you downloaded the data, your regressions might look completely different.
- Rewriting in one example firm:



# Stock returns (predictive panel regressions)

Data version	09/2018	09/2020	03/2021	09/2018	09/2020	03/2021
Dependent variable	<i>Future Return</i>	<i>Future Return</i>	<i>Future Return</i>	<i>Future Return</i>	<i>Future Return</i>	<i>Future Return</i>
	(1)	(2)	(3)	(4)	(5)	(6)
<i>E&amp;S Score</i>	0.001 (0.06)	<b>0.031**</b> <b>(2.43)</b>	<b>0.030**</b> <b>(2.31)</b>			
<i>E&amp;S Score Top 25%</i>				0.892 (1.56)	<b>1.170**</b> <b>(2.09)</b>	<b>1.332**</b> <b>(2.33)</b>
Observations	20,874	20,874	20,874	20,874	20,874	20,874
Control variables	Yes	Yes	Yes	Yes	Yes	Yes
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Industry Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Country Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Adj. R-squared	0.12	0.12	0.12	0.12	0.12	0.12

Source: Berg, Fabisik, Sautner (2020)

Thank you for your attention!