California Management Review

CORPORATE SOCIAL RESPONSIBILITY

Is ESG Simply the Old CSR Wine in a New Bottle?

by Nives Dolsak, Jennifer J. Griffin, and Aseem Prakash

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ESG initiatives will provide little social value if firms do not improve conditions that led CSR to fail.

INSIGHT | OPINION 15 May 2022

The **2022 Edelman Trust Barometer**, which surveyed 36,000 respondents across 28 countries, **reports** that 61 percent of international respondents identify businesses as trusted institutions.

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These results **indicate** that businesses are slightly more trusted than NGOs, at 59 percent, and substantially ahead of governments, at 52 percent.

These results are surprising because populists often demonize businesses, blaming them for problems ranging from climate change to increasing social inequalities.

How should businesses respond to the Edelman survey results? Declare victory and march on? Or work harder to create "value" as institutions working to address pressing social challenges?

This dilemma begs the question of how to define "value." The short answer is that businesses **create** value by aligning their actions with societal priorities and profits follow. But it is not clear what these societal priorities are and who decides them. Citizens elect governments to make public policy reflecting societal priorities—but no one elects corporations.

This is where the environmental, social, and governance (ESG) movement comes in. ESG is a framework that **identifies** societal priorities for firms in those three broad areas. Moreover, ESG metrics can guide managerial action while **signaling** to external constituencies a credible commitment to aligning managerial action with societal priorities.

But the ESG movement sounds like the older **corporate social responsibility** (CSR) movement—but with a new name.

By many estimates, CSR—in which companies **integrate** social concerns into their business strategy and operations via stakeholder engagement—has yet to **transform** firms to innovate. But if firms do not fix the harms that motivate CSR initiatives, should we expect ESG to do better?

At the core of the alphabet-soup debate about ESG and CSR **remains** the question about the economic and social purpose of modern corporations, in terms of what value they create and how they create it.

Ever since the limited liability firm **emerged**, this question has dodged business managers and ethicists alike. The modern corporation emerged in response to technical and financial imperatives of mass-production technology that required **mobilizing** vast quantities of capital from the public––a task beyond the reach of traditional family-owned firms. Moreover, these new conditions necessitated a professional-managerial class to **manage** the modern corporation in a market rife with competition.

As a result, modern corporations **run** under technically proficient managers working on behalf of shareholders who contributed capital to establish the firm. This is not to say all shareholders have similar preferences. For example, shareholders might **prefer** different time horizons over which to maximize their wealth. With efficient stock markets, unhappy shareholders can **exit** firms by selling off shares.

This narrow view that a firm's sole purpose is to maximize shareholder wealth has **faced** considerable pushback for decades. The reality is that firms can **operate** effectively only with active buy-in from multiple stakeholders: the political system for permits and land purchases as well as suppliers, investors, employees, neighbors, and customers.

Without social and political buy-in, firms cannot **perform** tasks, innovate, grow, or even deliver a return on shareholders' investment. Ironically then, it is in firms' self-interest to function in conjunction with multiple stakeholders to **secure** autonomy to operate.

But an expansive stakeholder view poses problems as well. Not all stakeholders are alike. And unlike shareholders, some stakeholders may not be able to pack up and leave. Given the high cost of exit for some stakeholders, including some shareholders, they may **exercise** their voices and impede the everyday work of the firm. This broader view of the firm, then, presents challenges for how firms identify and engage with critical stakeholders to create value for all.

This is where CSR and ESG come in and offer productive frameworks for stakeholder engagement.

The older CSR movement **originated** in the 1950s with **Howard R. Bowen's** book, ***Social Responsibilities of the Businessman***. It received a boost in 2000 when the UN Secretary-General at the time, **Kofi Annan**, launched the **United Nations Global Compact**, which encouraged firms to adopt socially beneficial practices. But without a metric to assess firms' CSR performance, after the initial excitement, the Global Compact today seems **destined** to join the ranks of failed efforts to "reform" corporations.

The lesson from CSR is that both managerial accountability and public trust **suffer** without clear metrics for who benefits, how much scarce time and money is invested, how long that time and money is invested, and how much social impact results. The metric deficit of CSR has, in part, contributed to the more recent popularity of ESG.

ESG **promises** to outline a monetized metric to assess firms' performance toward its environmental impacts, social impacts, and internal governance systems. But unlike quarterly profits guiding shareholder maximization, there is no singular, widely **accepted** ESG metric and no credible oversight. As a result, actors operationalize ESG differently, ranging from a narrowly defined ESG for investors to a more broadly defined, holistic view of environmental impacts and social well-being. This lack of consensus **creates** the possibility of green-washing and, more broadly, ESG-washing.

Although several organizations, such as the **Chartered Financial Analyst Institute**, are developing ESG investment certificates and standards, ESG remains in a fuzzy zone, led more by rhetoric than by measurable performance.

Viewed this way, narrowly defined ESG investing does not provide substantially superior guidance to managers or investors than CSR did.

When conflicts occur among ESG's different components, it remains unclear how firms should prioritize, integrate, or innovate to manage tradeoffs across environmental, social, and governance goals. If ESG proponents **fail** to address the fundamental issues of defining value creation, for whom and how value is created, and which priorities should prevail, they will repeat the mistakes of CSR.

ESG rhetoric can garner credibility for firms for a limited time only. Given the climate crisis and persistent public health and social inequities demanding business solutions—not to **mention** the blessing of BlackRock CEO Larry Fink—ESG is now fashionable. But fashion, just like trust, can be fleeting. When the next recession arrives and firms must cut discretionary expenses, ESG will go if it is considered an expense rather than an integral investment in the firm's future growth.

Without a strong link to business's core purpose and a coherent ESG narrative that creates value and enjoins a broad array of stakeholders, ESG will become empty talk. As of now, ESG **conveys** a virtue signal, with a "trust me" message that does little to reshape how firms create value and gain public trust.

*Note: This essay was previously published in **The Regulatory Review**, March 28, 2022*

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