

The Journal of Finance®



Laura T. Starks

The President of the American Finance Association 2022

Presidential Address: Sustainable Finance and ESG Issues—*Value* versus *Values*

LAURA T. STARKS*

ABSTRACT

In this address, I discuss differences across investor and manager motivations for considering sustainable finance—*value* versus *values* motivations—and how these differences contribute to misunderstandings about environmental, social, and governance investment approaches. The finance research community has the ability and responsibility to help clear up these misunderstandings through additional research, which I suggest.

WHILE SUSTAINABLE FINANCE HAS BEEN drawing increased attention from institutional and retail investors, regulators, politicians, corporate leaders, and employees, alike, there is no clear consensus on the meaning of sustainable finance or the acronyms associated with it—ESG (environmental, social, and governance), SRI (socially or sustainably responsible investing), and CSR (corporate social responsibility). The lack of clarity on the meaning of these terms leads to misunderstandings about how they affect investors, corporations, and asset markets, which can make it difficult to interpret evidence on investment behavior and to design related regulations. In this address, I argue that the misunderstandings arise from differences in investors' and managers' motivations. In particular, I argue much of the confusion is due to differences in whether motivation arises from *value* or *values*, that is, from regarding the

*Laura T. Starks is with McCombs School of Business, University of Texas at Austin. For helpful comments, I would like to thank the editor, Antoinette Schoar, as well as Reena Aggarwal, Andres Almazan, Natasha Burns, Eli Fich, Stuart Gillan, John Graham, John Griffin, Andy Koch, Jeff Netter, Clemens Sialm, Rick Sias, Sheridan Titman, Parth Venkat, and Qifei Zhu. For excellent research assistance, including commenting on drafts, I would like to thank Linda Du, Alex Priest, and Lin Yang. I have read *The Journal of Finance's* disclosure policy and have no conflicts of interest to disclose.

Correspondence: Laura T. Starks, McCombs School of Business, University of Texas at Austin, Austin, TX 78712, USA; e-mail: laura.starks@mcombs.utexas.edu.

This is an open access article under the terms of the [Creative Commons Attribution-NonCommercial-NoDerivs](#) License, which permits use and distribution in any medium, provided the original work is properly cited, the use is non-commercial and no modifications or adaptations are made.

DOI: 10.1111/jofi.13255

© 2023 The Authors. *The Journal of Finance* published by Wiley Periodicals LLC on behalf of American Finance Association.

ESG qualities of an investment as important to its financial *value* or, as consistent with one's *values*.¹

Because of the misunderstandings about investors' and managers' motivations, people often talk at cross purposes about ESG. Therefore, it is incumbent upon the finance research community to provide clearer analyses and interpretations of these issues from a financial economics perspective.² In particular, finance researchers have an opportunity to make important contributions to the literature and society by conducting research that considers both pecuniary and nonpecuniary aspects of ESG, taking an objective stance with regard to the incentives, costs, and benefits related to sustainable finance, and that provides evidence on the associated economic implications. In this address, I highlight areas of ambiguity where more research could provide clarity.

As I note above, the terminology related to sustainable finance is a central issue—what terms should be used to describe these types of approaches to manager or investor decision making? Some people prefer sustainability, while others prefer responsible investing, ESG, or CSR, yet, there is no clear understanding of how these terms differ or even what a given term means. For example, the term “sustainability” has a variety of meanings depending on the context. To some, the term's principal focus corresponds to the environment. To others, the term refers to the broader idea of sustainability for people, planet, and profit. To still others, the term's meaning encompasses not only people and planet, but also prosperity, peace, and partnerships.

Until we see more agreement on what the various sustainability terms mean, existing research needs to be considered in light of how authors frame the research question. Moreover, while a large body of outstanding research has improved our understanding of ESG and related topics, many questions remain open. My aim here is to focus on moving this field forward, by drawing attention to the misunderstandings that have arisen so future financial economics research can clear up these misunderstandings and provide deeper theoretical and empirical analyses of ESG. Note that I spend relatively little time on the “G” or governance aspect of ESG because our field has a long tradition of investigating corporate governance issues. I do briefly discuss, however, important unanswered questions related to the governance areas of ESG.

For some investors and managers, ESG decision making is driven by *values*, that is by preferences—in particular, nonpecuniary preferences. A variety of motivations can lead to a *values* approach, for example, a desire not to support businesses associated with objectionable products or conduct or a desire to support businesses that reflect their own religious values. Differentiating these motivations is challenging because nonpecuniary preferences vary across investors and managers, leading to differences in priorities

¹ Because “ESG” has become the dominant shorthand used to refer to these concepts, for brevity I rely largely on this shorthand throughout.

² As I was writing this address over the 2022 calendar year, others were developing and publishing ideas some of which are similar to those that I propose in this address. In particular, Edmans (2022) and Pollman (2022) have written thoughtful pieces on ESG.

across areas of concern such as carbon footprints, harm to animals, and child labor.³

For other investors and managers, ESG decision making is driven by financial *value*, that is, by a firm's risk and return opportunities. The *value* approach differs conceptually from the *values* approach in both intent and operationalization. For example, ESG considerations can shed light on financially significant risks including environmental, reputation, human capital, litigation, regulatory, corruption, and climate risk, among others.

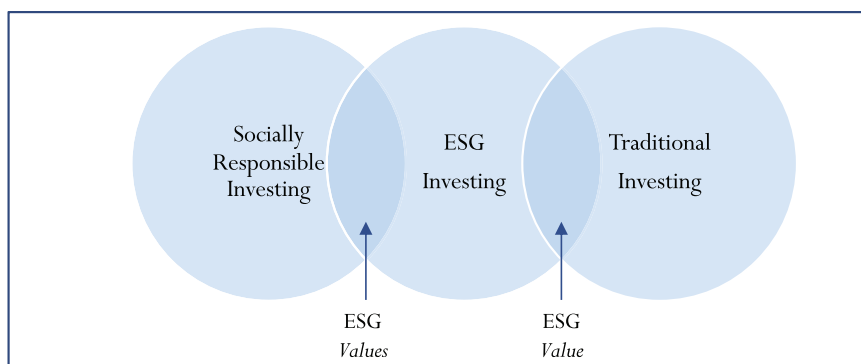
As academic researchers, we need to better account for the distinction between ESG *values* and *value*. Clear identification may be complicated by the fact that ESG investing can also be motivated by a combination of *values* and *value*. One can think of the range of ESG investment approaches as captured by a linear Venn diagram. As Figure 1, Panel A, shows, ESG investing can be important to both investors focused on socially responsible investments and traditional (i.e., financially oriented) investors. On the one hand, SRI investors may consider ESG investment primarily from a *values* perspective. On the other hand, financially oriented investors who employ an ESG approach do so from an exclusively *value* perspective.

In Figure 1, Panel B, I add impact investing to the Venn diagram. This figure illustrates the full spectrum of investment approaches and the relation of each to investors' preferences and financial value considerations.⁴ Impact investors have an intentional focus on the environmental and social outcomes of an investment.⁵ Closely related is SRI, where investors' main intent is to avoid supporting companies that do not reflect their values. Removing such companies from their portfolios, that is, negative screening, therefore serves as the primary investment focus of SRI strategies. The next strategy along the spectrum, ESG investing, is what could be arguably referred to as the "classic" form of sustainability investing. This strategy can include both nonpecuniary and pecuniary motivations, depending on the investor's *values* versus *value* orientation. For some investors, ESG investment primarily represents a way to express their nonpecuniary preferences, similar to SRI investors, but often using positive screening, that is, including companies in their portfolios that reflect their values. In contrast, for other investors, ESG investment means considering the ESG aspects of the firm to mitigate risks and enhance returns. A variety of strategies can be employed under this approach such as ESG integration, positive ESG tilt, negative ESG screening, and ESG risk management,

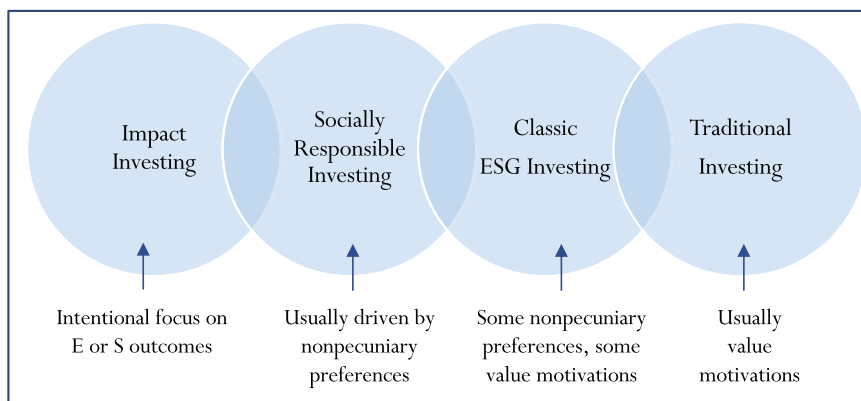
³ For discussions on the history of investing based on *values*, see, for example, Renneboog, ter Horst, and Zhang (2008) and Starks (2021).

⁴ Consistent with the terminology confusion discussed above, ESG investing could also be shown as encompassing both SRI and impact investing. I have displayed them as distinct in order to highlight the differences.

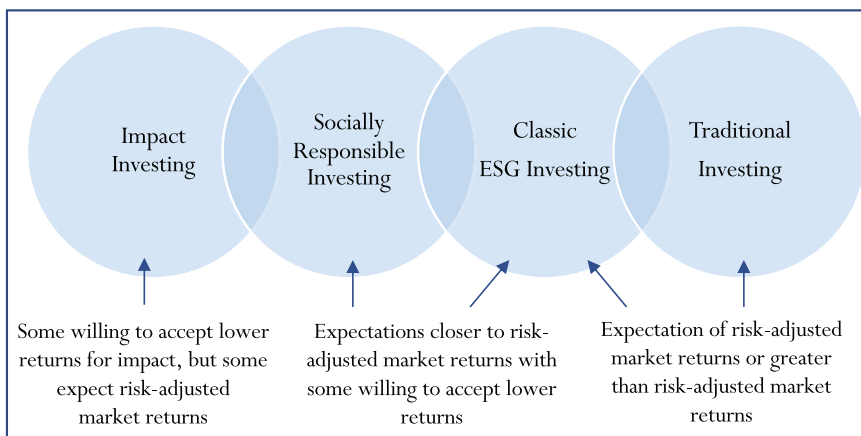
⁵ Impact investing usually involves expectation of receiving both financial and social returns, where the social returns are based on both intentionality and additionality.



Panel A. *Values* versus *Value* in Investment Approaches



Panel B. *Values* versus *Value* in Investment Approaches: Investor Preferences



Panel C *Values* versus *Value* in Investment Approaches: Expected Returns

Figure 1. *Values* versus *value* in investment approaches. This figure illustrates a Venn diagram for the spectrum of investment approaches. Panel A shows the interlap between SRI, ESG, and traditional investing; Panel B shows the typical investor preferences related to the approaches; and Panel C shows the typical expected returns across the approaches. (Color figure can be viewed at wileyonlinelibrary.com)

among others.⁶ The final investment strategy along the spectrum is traditional investing, where interest is on risk and return alone.

Figure 1, Panel C, adds to the Venn diagram the expected return expectations of the different investment approaches. For impact investors, these expectations can span from being willing to give up returns in exchange for meeting nonpecuniary goals to an expectation of earning risk-adjusted market returns, see Barber, Morse, and Yasuda (2021) for estimates of the impact investors' willingness-to-pay (WTP). Expected return requirements can also vary within and across the other investment approaches, with some ESG investors, particularly those in the SRI spectrum, again showing measurable WTP (e.g., Baker, Egan, and Sarkar (2022)). In sum, as the figure illustrates, there exists a large degree of heterogeneity within each of these investment approaches.

The remainder of the address is organized as follows. In Section I, I first discuss the growth in interest in, and the evidence we have regarding, investors' and managers' *value* or *values* motivations for ESG investing, including what can be inferred from country differences. In Section II, I summarize some of the research regarding ESG investment performance and make the point that before we can draw definitive conclusions on such performance, we need to separate the influences of *value* versus *values* investors more cleanly. In this section, I also discuss the difference between investors' concerns about ESG risks in firms' business processes (of most importance to *value* investors) and the effects of those processes on the environment and the communities in which the firms operate (often the primary focus of *values* investors). Much of the work on ESG has focused on equities, but we should consider these issues in other asset classes, which I briefly discuss. Also relevant to this discussion is the framing of ESG issues and why the three aspects should or should not be aggregated into one overarching concept. In Section III, I focus on the relation between *value* and *values* investing, and a topic of particular importance today, namely, environmental issues, including climate risk. In Section IV, I turn to the role of owners, that is, the use of voice and exit, and the consequences of these choices. In Section V, I provide a brief discussion of social and governance issues. Finally in Section VI, I give some concluding remarks.

I. Growth in Interest in and Motivations for ESG Investing

Over the last decade, there has been substantial growth in interest in the concept of ESG. Figure 2 provides a worldwide Google Trends plot for the Google-set topic of "Environmental, Social and Corporate Governance." The figure demonstrates that interest in ESG, as reflected by individual Google

⁶ Since negative ESG screening is a primary investment technique of *values* investors, one may argue that it can be interpreted as evidence of *values* investors. However, it can also be employed by *value* investors. I discuss this more thoroughly in Section IV.B, where I discuss divestment issues.

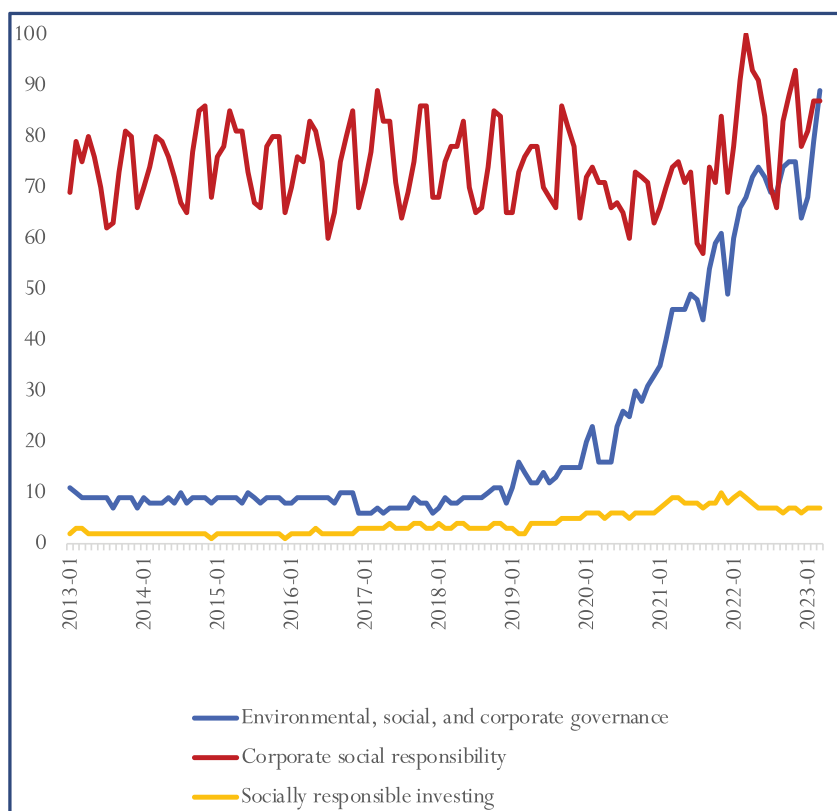


Figure 2. Increasing interest in ESG according to Google Trends. This figure illustrates the time-series trends for worldwide searches for the Google search topics: “environmental, social and corporate governance,” “corporate social responsibility,” and “socially responsible investing” from January 2013 to January 2023. (Color figure can be viewed at [wileyonlinelibrary.com](https://onlinelibrary.wiley.com))

searches, has been growing rapidly, particularly in the last five or so years. This result can be compared to the Google-set topic “Corporate Social Responsibility,” which has remained a relatively important topic over the past decade. In contrast, while the Google-set topic “Socially Responsible Investing” has been of sufficient interest to also warrant designation as a Google Trends topic, it has remained a relatively minor focus of Google searches as compared to the other two topics.

The increasingly broad interest in ESG investing can also be illustrated by examining time-series differences in U.S. active mutual funds’ percentage ownership for high- and low-ESG firms. To conduct this analysis, each year, I sort S&P 500 Index firms into ESG quartiles according to their S&P Global ESG scores and then calculate the fraction of their shares held by actively managed domestic equity mutual funds that are *not* identified as ESG funds according to the Morningstar designations. In Figure 3, Panels A to E show the increas-

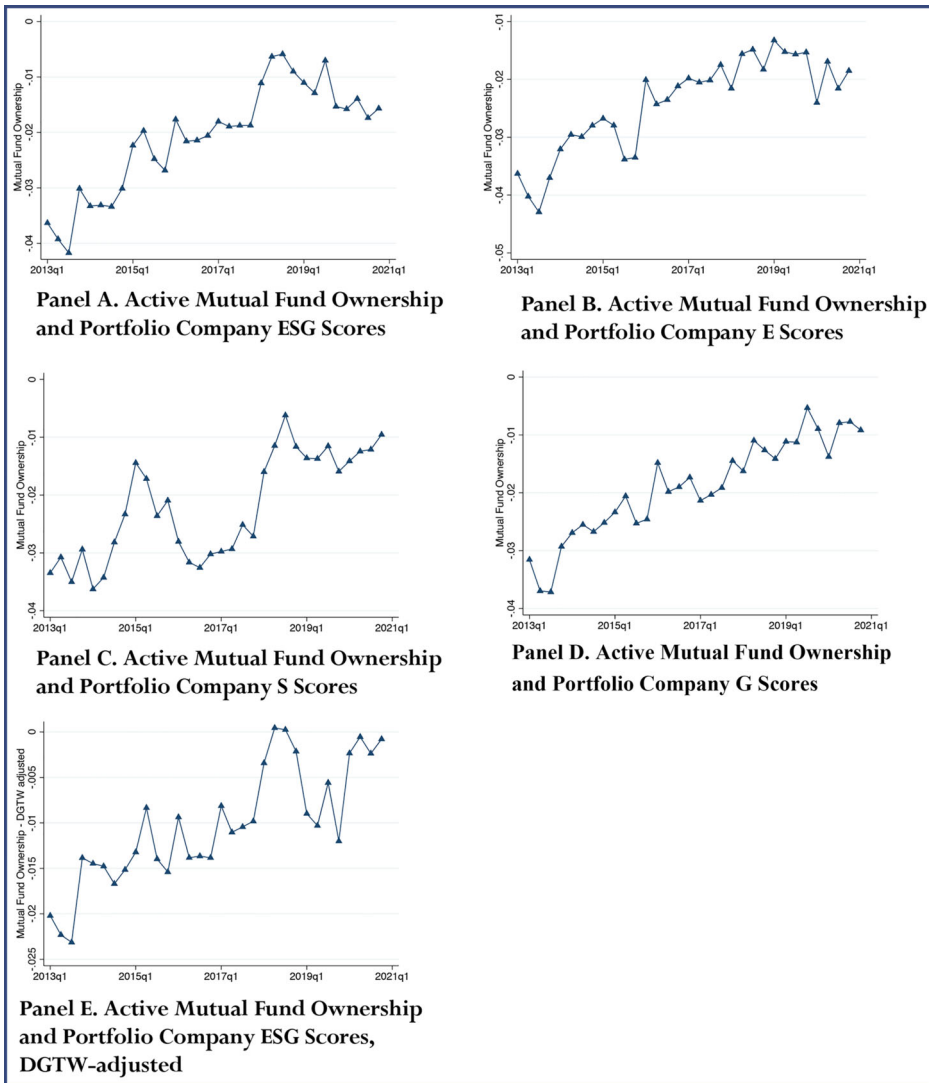


Figure 3. Active mutual fund management and portfolio company ESG scores. This figure shows differences over time between active mutual fund ownership in the highest S&P Global ESG score quartile of S&P 500 firms and that in the lowest quartile, where scores are annually updated. Panel A plots results for total ESG scores, Panel B for E scores, Panel C for S scores, Panel D for G scores, and Panel E for ESG scores with DGTW characteristic adjustments. (Color figure can be viewed at wileyonlinelibrary.com)

ing interest in ESG qualities by conventional mutual fund portfolio managers. Panel A shows the differences in each quarter between the active mutual fund ownership of firms in the highest ESG quartile versus the firms in the lowest ESG quartile. Although conventional mutual funds hold a larger fraction of shares in low-ESG companies throughout the period, there is a clear trend

of increasing ownership in the high-ESG firms relative to the low-ESG firms. Moreover, this increasing pattern continues to hold in Panels B to D, which show the differences for the E, S, and G scores separately. Since the relation between mutual fund ownership and firm characteristics changes over time (Bennett, Sias, and Starks (2003)), in Panel E, the ownership percentages for the ESG scores are adjusted each year for the Daniel et al. (1997) (Daniel, Grinblatt, Titman, and Wermers [DGTW]) characteristics.⁷ The increasing pattern remains generally the same as in Panel A. The increasing ownership patterns do not appear explainable by industry rotations or other factors. To differentiate the motivations between *value* and *values* investors, we need to better understand the determinants of this secular shift.

A. Investor Motivations for ESG Investing

To understand the growth of interest in ESG investing as well as the effects of this investment approach, we first need to distinguish investors' motivations. As discussed above, the motivations of *value* investors center on how considering ESG issues can help drive firm value, that is, improve the firm's risk-return prospects. These investors not only use information on a firm's ESG qualities in their investment decisions, but also often engage firm management on these issues to help obtain lower risk or enhanced returns. In contrast, the motivations of *values* investors arise from their nonpecuniary preferences. In general, *values* investors do not want to hold a firm's shares if the company is associated with objectionable products or behaviors, that is, they do not want to supply capital to or profit from such firms. These investors also tend to be particularly interested in the effects of the corporation on society and the environment, and hence they too sometimes try to achieve their goals by engaging firm management, either directly or by voting their proxies. Of course, as noted above, some investors are simultaneously a *values* and a *value* investor and hence employ multiple strategies simultaneously.

The increasing practitioner interest in ESG risks has been accompanied by a growing body of academic research, including theoretical work. Many ESG theory papers can be sorted into two groups. One features *values* investors with nonpecuniary preferences who buy ESG stocks versus their counterparts who are solely financial investors.⁸ Typically the weightings on the proportion of investors with nonpecuniary preferences are important in the equilibrium considerations. The other group of common theoretical studies feature at least some *value* investors who have primarily financial motivations for ESG invest-

⁷ The DGTW adjustments were made as follows. First, assign the DGTW groups (portfolios) to each stock according to DGTW (1997). Next calculate the ownership for each stock-quarter from the non-ESG actively managed domestic equity mutual funds in the sample. For each DGTW portfolio-quarter, calculate average ownership across stocks by the mutual funds and then for each stock-quarter, subtract the mean corresponding DGTW portfolio-quarter mutual fund ownership.

⁸ The theories employ different terminology, for example, ESG, CSR, and green and brown investors.

ments.⁹ We need more theory here. For instance, we need additional theoretical frameworks that consider the range of differences in motivations within the *value* and *values* ESG investor groups. For example, are the two types of investors complementary to each other or do they compete with each other, and how does the distribution of *values* versus *value* ESG investors impact asset prices? Although some of these questions have been explored in the context of so-called green versus brown investors, they have not been explored in depth with regard to *value* versus *values* ESG investors from multiple theoretical frameworks.¹⁰

Recent research examines the question of ESG motivation through surveys, experiments, and archival data. For example, recent studies provide important insights by focusing on Dutch investors and pension fund participants. Based on a survey and experimental data, Riedl and Smeets (2017) conclude that the primary motivation for investors to hold SRI funds arises from social preferences and social signaling, and that financial motivations, while a factor, are of more limited importance to these investors. In an experiment on pension fund participants, Bauer, Ruof, and Smeets (2021) find that a majority of the participants think that their pension fund should engage in more responsible investing activities based on the participants' social preferences rather than their financial motivations. In another experimental study, Brodback et al. (2022) conclude that investors' WTP for SRI increases in investors' altruism. These three studies focus on why individuals would choose to invest in SRI. Humphrey et al. (2022) also employ an experimental setting, but take a different perspective and examine how investor preferences enter into individuals' return beliefs and asset allocation decisions. The results point to an asymmetry in the relationship between investor preferences and investment decisions, with negative externalities in social outcomes having greater weight than positive externalities in the asset allocation decision. Hoepner, Majoch, and Zhou (2021) contribute to our understanding of investor motivation by empirically showing that one of the factors affecting the decision to sign on to the Principles of Responsible Investment (PRI) relates to home-country cultural norms.¹¹

A recent survey of Vanguard retail investors relates ESG preferences to investors' portfolio holdings (Giglio et al. (2023)). For the Vanguard sample, the authors find a mix of motivations, with 45% not seeing any specific reason to invest in ESG stocks, while 25% are primarily motivated by ethical consider-

⁹ See, for example, Baron (2007, 2008), Fama and French (2007), Benabou and Tirole (2010), Heinkel, Kraus, and Zechner (2001), Albuquerque, Koskinen, and Zhang (2019), Chowdhry, Davies, and Waters (2019), Pastor, Stambaugh, and Taylor (2021), Pedersen, Fitzgibbons, and Pomorski (2021), Baker, Hollifield, and Osambela (2022), Goldstein et al. (2022), Berk and van Binsbergen (2022), Edmans, Levit, and Schneemeier (2022), Oehmke and Opp (2022), and Zerbib (2022).

¹⁰ Pedersen, Fitzgibbons, and Pomorski (2021) is one example of a theory with both *value* and *values* ESG investors.

¹¹ For additional work on ESG investor motivations, see Bonelli, Briere, and Derrien (2022), Bonnefon et al. (2022), Brodback, Guenster, and Mezger (2019), and Heeb et al. (2023).

ations, which under my interpretation implies that these investors are *values* investors. About 7% of investors in the Vanguard sample believe that ESG investments will outperform the market. In my framework these are *value* investors. The 25% who believe that ESG investments hedge climate risk could be *value* or *values* ESG investors. Giving substance to the credibility of the survey responses, the authors find that the investors' portfolio allocations line up with their beliefs.

Baker, Egan, and Sarkar (2022) examine ESG investor motivations by measuring investors' WTP for ESG mutual funds and ETFs. Their evidence suggests that investors are willing to give up some return for sustainable investments. If one considers the authors' WTP measure an average across both *values* and *value* investors, then the estimated WTP of the *values* investors should be even higher.

However, not all investors are willing to give up returns to make sustainable investments. For example, as Giglio et al. (2023) find, some of their sample investors believe that they will earn higher returns from ESG investments. Further evidence is provided by Barber, Morse, and Yasuda (2021). Using random utility/WTP models and private equity fund data, they find that, on average, investors are willing to accept expected returns on impact investments that are 2.5 to 3.7 percentage points lower than market returns, depending on the investor. However, while some institutional investor categories such as public pension plans are willing to give up return for impact investing purposes, other institutional investors in their sample such as private pension plans are not. Thus, some investors want to invest in impact activities while earning closer to a market-adjusted rate of return.

Empirical evidence suggests that both *value* and *values* motivations contribute to the choices of retail and institutional investors. Several studies find that ESG mutual funds exhibit less flow-performance sensitivity than other types of mutual funds, which suggests that systematic differences exist across ESG and non-ESG investors.¹² Based on evidence from the introduction of Morningstar Globe Ratings as well as survey evidence, Hartzmark and Sussman (2019) conclude that either investors have expectations of future performance from sustainability or investors' nonpecuniary motives influence their investment decisions.¹³ However, Gantchev, Giannetti, and Li (2022b) provide evidence inconsistent with the Globe Ratings having an impact due to investors' nonpecuniary motives. They find that less than a year after Morningstar introduced its sustainability rankings, fund flows stopped being affected by changes in the ratings. They conclude that investors in funds

¹² See, for example, Bollen (2007), Benson and Humphrey (2008), Renneboog, ter Horst, and Zhang (2011), Bialkowski and Starks (2018), and El Ghouli and Karoui (2017).

¹³ Ammann et al. (2018) also find a change in flows after the introduction of the Morningstar sustainability rankings. Similarly, Ceccarelli, Ramelli, and Wagner (2022) find that when Morningstar introduced their carbon risk metrics, the low-carbon funds experienced a significant increase in flows, and they find this reaction to be stronger when combined with funds' high risk-adjusted returns.

without an explicit sustainability objective consider return performance to be more important.¹⁴

As discussed earlier, *value* investors consider ESG factors because of the perspective they provide on risks and return opportunities. These investors have a general expectation that incorporating ESG issues in their investment decisions will result in lower risk or higher returns, whether through portfolio selection or firm engagement (e.g., Dimson, Karakas, and Li (2015, 2021), Krueger, Sautner, and Starks (2020), Barber, Morse, and Yasuda (2021), Hoepner et al. (2022)). Starks, Venkat, and Zhu (2022) find that longer term investors have stronger preferences for the higher rated ESG stocks as compared to other investors and they provide evidence suggesting these preferences are due to firm value considerations. However, whether such investments actually fulfill these expectations is a matter of some debate, which I discuss further below.

Surveys of institutional investors also provide insights with regard to the *values* versus *value* motivations. For example, Krueger, Sautner, and Starks (2020) find no single overarching motivation for institutional investors to incorporate climate risk into their portfolio decisions. Rather, they find a mix of pecuniary and nonpecuniary motivations. Of the seven highest ranked reasons for incorporating climate risk (measured in terms of the percentage of respondents viewing the issue as important), three are primarily financial (improves investment returns, reduces portfolio risks, and reduces tail risks), two are primarily nonpecuniary (moral/ethical considerations and reflect asset owners' preferences), and two have a blend of financial and nonfinancial implications (protection of investors' reputations and legal/fiduciary duties).

B. Manager Motivations for ESG Investing

Beyond a better understanding of investors' ESG motivations, we also need more in-depth analysis of corporate boards' and managers' motivations. This analysis is particularly important given frequent claims of corporate greenwashing. Reviewing previous corporate finance research on ESG or CSR reveals that many of the studies in this area have conflicting hypotheses and results (Gillan, Koch, and Starks (2021)). In particular, the empirical evidence on the relationship between a firm's ESG/CSR profile and activities and its markets, leadership, ownership characteristics, risk, performance, and value is quite mixed.¹⁵ In addition, there exists some evidence that managers respond to investor demand for ESG. For example, with a focus on investor demand for beneficial environmental actions Gillan, Sekerci, and Starks (2022) find that firm ownership plays an important role in managers' response to investor

¹⁴ Additional studies on ESG ratings and stock returns include Brandon Gibson, Krueger, and Schmidt (2021) and Berg et al. (2021).

¹⁵ Whether a business should pay particular attention to environmental and social issues (or whether they should practice social responsibility) has been a subject of debate among finance academics and practitioners for many years. For examples of earlier contributions, see Starks (2021).

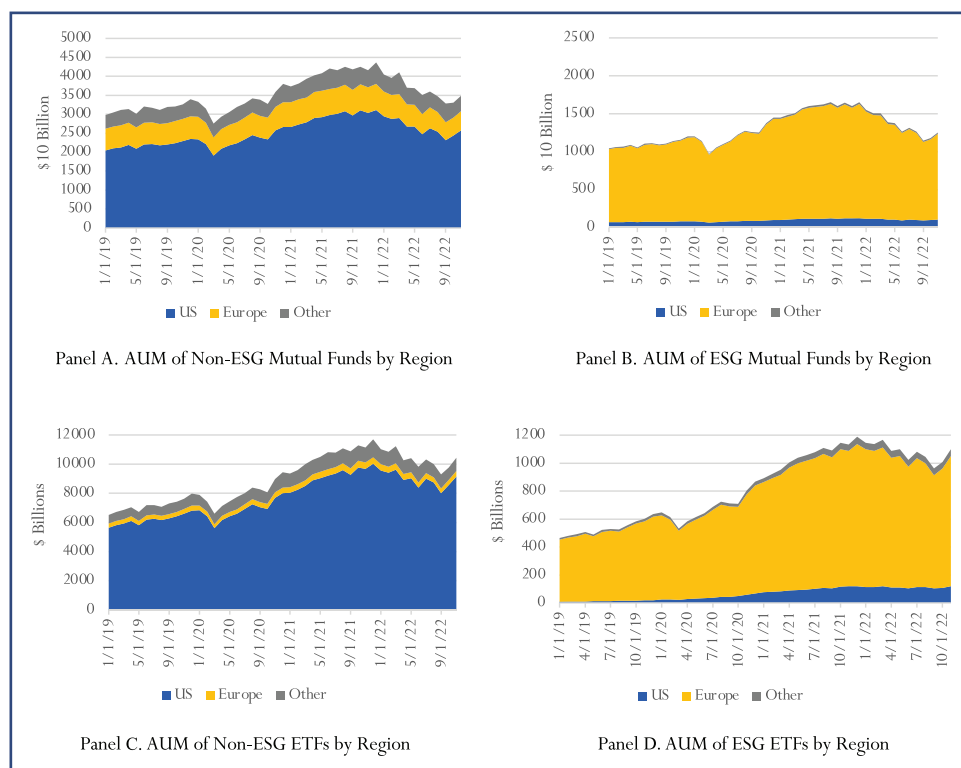


Figure 4. Geographic differences in ESG fund assets under management (AUM). These figures show the changes in AUM from January 2019 to December 2022 for ESG and non-ESG mutual funds (Panels A and B) and ETFs (Panels C and D) as designated by Morningstar for the United States, Europe, and other regions. Note that these figures are on different scales. (Color figure can be viewed at wileyonlinelibrary.com)

demand for higher environmental profiles—firms with more powerful owners respond more to the investor demand.

An important implication of these analyses is that if managers become more environmentally friendly to lower their cost of capital to satisfy *values* investors, then securities may be affected by a “greenium.” However, if sufficient investors in corporate securities are driven by *value* considerations, then firms’ stocks and bonds should be priced fairly.

C. Motivations and Country Cultural Differences

Examining assets under management (AUM) and flows into ESG funds versus non-ESG funds across geographies can provide further insights into not only the increasing interest in ESG but also differences in investor motivations. In Figure 4, Panels A and B show the AUM for an international sample of mutual funds designated by Morningstar as ESG and non-ESG. Panels C

and D show the AUM for the international exchange-traded fund (ETF) market similarly divided into ESG and non-ESG funds. In Panel A, the blue area shows the AUM in U.S. non-ESG-designated funds, the orange area shows the amount for European funds, and the grey area shows the amount for other regions. As can be seen, the U.S. mutual fund market is the largest mutual fund market overall in terms of AUM. This contrasts sharply with the relative AUMs in Panel B, which shows that the European market is by far the largest market for ESG mutual funds. Panels C and D demonstrate the same patterns for the ETF market. While the ESG funds' AUMs in both the U.S. and European markets have been generally growing over time, due to both increased flows and increased returns, the differences in the geographic locations of the relative amount of ESG versus non-ESG investment are striking. The implication is that on a relative basis, the European mutual fund and ETF markets have many more investors interested in ESG funds than do the U.S. or other markets. The question that then arises is why this difference occurs. I argue that the explanation most likely comes back to the differences between the ESG investing motivations of *values* and *value* investors.

The geographic differences shown in the growth patterns of the ESG fund markets also extend to differences in company policies and actions with regard to ESG issues. In Figure 5, Panels A to C show raw and industry-adjusted S&P E, S, and G scores averaged across companies in each country. The panels point to strong cross-country and regional differences in these scores.

Figure 6 provides a color-coded map of the average E score across countries, where dark green indicates the highest average scores. The figure clearly demonstrates strong regional differences in the average E scores, with European firms often performing better along the dimensions of E scores. This finding is consistent with evidence from John Graham's (2022) presidential address in which he surveys executives and finds that European executives are almost twice as likely as their North American counterparts to consider the environment to be an important stakeholder.

These country and regional differences appear to be related to differences in governmental policies and actions with regard to the environment. Figure 7 plots the Yale country-level Environmental Performance Index (EPI) against the S&P E score by country.¹⁶ The Yale EPI measures 40 performance indicators across 11 issue categories to rank 180 countries on climate change performance, environmental health, and ecosystem vitality. Although some endogeneity most likely exists since country policies could affect company actions, the strong relationship shown in the figure and its accompanying correlation coefficient of 0.59 are still striking.

The country differences visible in the figures are consistent with underlying country characteristics driving differences in company ESG or CSR scores as suggested by Cai, Pan, and Statman (2016), who provide evidence that variation across countries is associated more strongly with country factors (per

¹⁶ See Wolf et al. (2022) for a discussion of the Yale EPI. In addition, Dyck et al. (2019) use the 2004 Yale EPI index to measure a country's environmental norms.

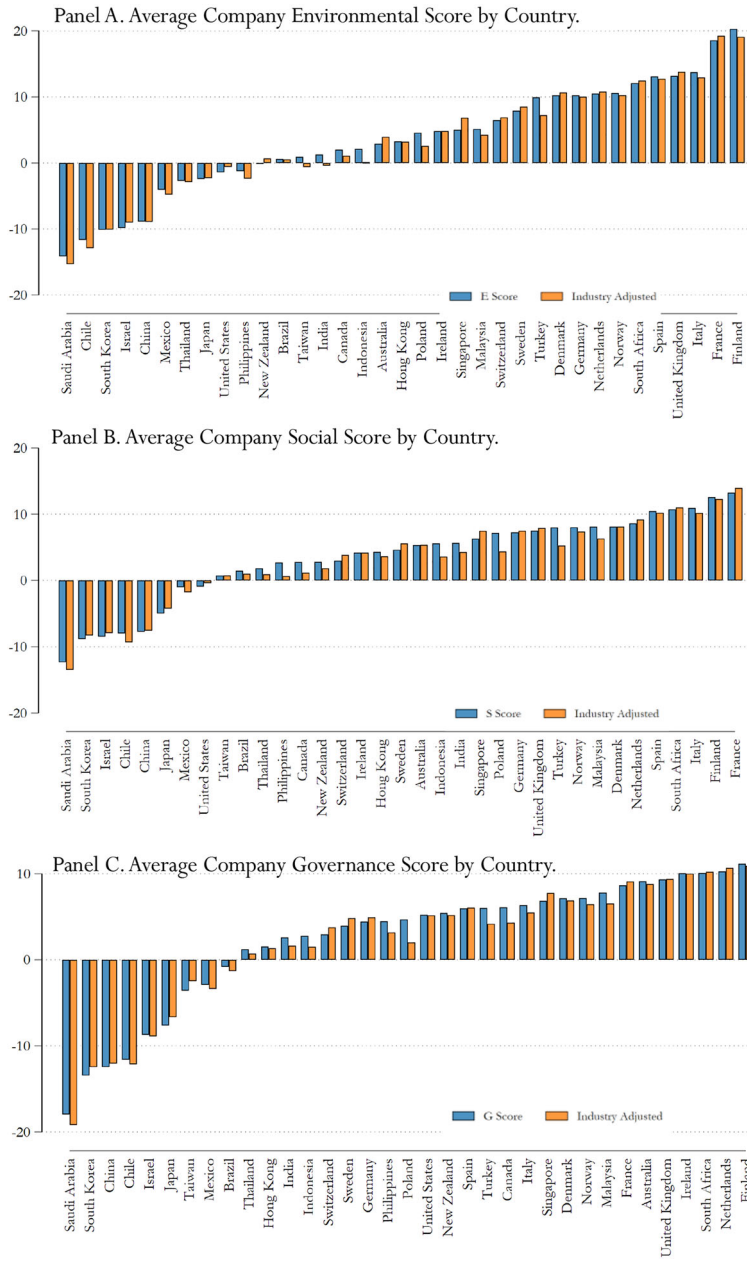


Figure 5. Average company environmental, social, and governance scores by country. Panel A shows average environmental scores, Panel B shows average social scores, and Panel C shows average governance scores for companies with available scores from S&P Global ESG scores. (Color figure can be viewed at wileyonlinelibrary.com)

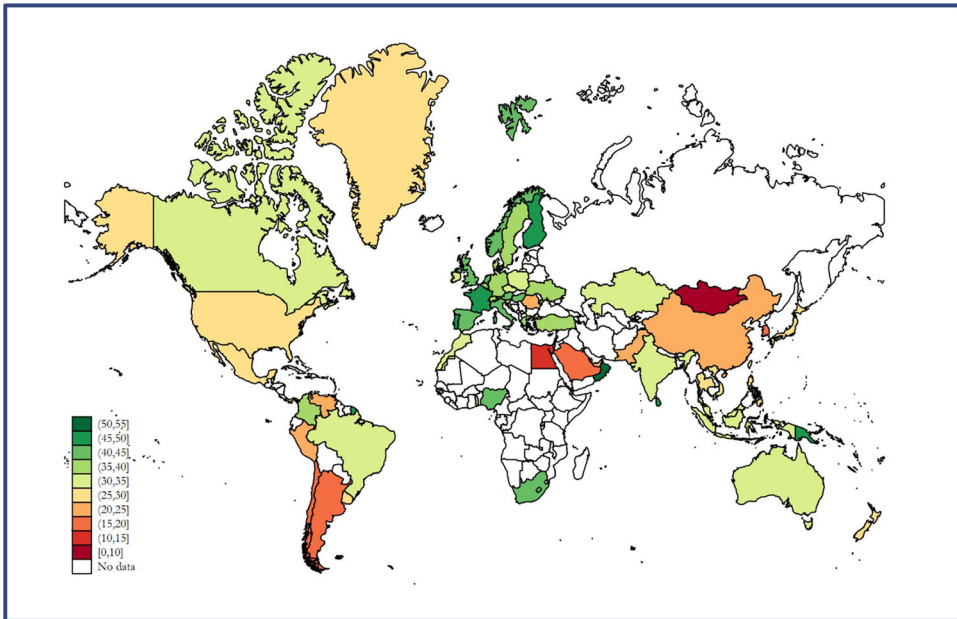


Figure 6. Environmental scores by country. This figure illustrates a color-coded map of environmental scores by country where the environmental scores are from S&P Global ESG scores. (Color figure can be viewed at wileyonlinelibrary.com)

capita income, the legal system, cultural harmony, and cultural autonomy) than with firm characteristics. Similarly, Liang and Renneboog (2017) conclude that a country's legal origin is the strongest predictor of firms' CSR adoption and performance.¹⁷ These results also suggest that beyond differences in management decisions, the differences in investors' ESG fund choices could be related to a country's cultural norms. In fact, Bialkowski, Starks, and Wagner (2022) find that the size of a country's ESG fund industry, whether measured relative to the size of the conventional fund industry or relative to the country's GDP, varies greatly across countries and is strongly related to the country's cultural norms. Perhaps not surprisingly, the authors also find that the ESG sector increases in the wealth of the country, as measured by GDP per capita. These figures are consistent with findings in Dyck et al. (2019) that institutional investors influence their portfolio firms' E and S performance and that these investors are from countries with cultural norms that emphasize E and S issues. In addition, the figures are consistent with the findings of Bose et al. (2023), who find that cultural differences affect the association they document between managers' climate-linked compensation and climate change impacts.

¹⁷ See also Doidge, Karolyi, and Stulz (2007), who find that country characteristics are more important than firm characteristics for corporate governance.

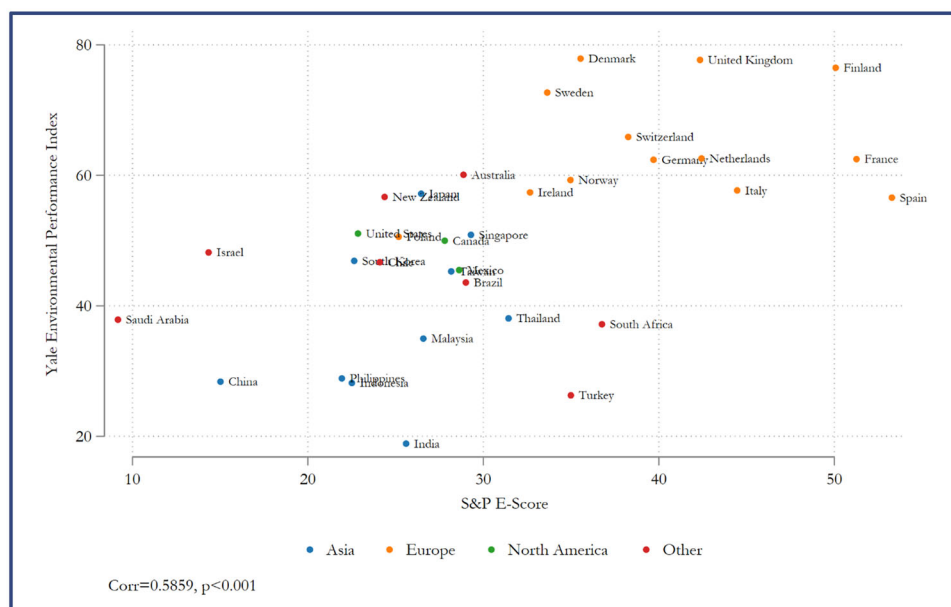


Figure 7. Yale Environmental Performance Index plotted against the S&P Global environmental score. This figure shows the 2022 Yale Environmental Performance Index per country plotted against the average S&P Global environmental scores for companies in the country. (Color figure can be viewed at [wileyonlinelibrary.com](https://onlinelibrary.wiley.com))

II. Value versus Values: Performance and Outcomes

A. ESG Investment Performance

One of the central concerns with ESG investing is the question of expected versus realized investment performance. The relationship between investment returns and ESG investing has been long debated. Again, arguments about returns from ESG investing depend on whether the premise corresponds to the *value* or the *values* perspective. Moreover, people have a tendency to interpret evidence according to their own beliefs (Nickerson (1998)).¹⁸

To address the question of ESG investment performance, one first needs to consider investors' expectations. As discussed earlier, *values* investors may have different return expectations than *value* investors. Since a *values* approach tends to rely on some form of negative screening, an investor using this approach faces a smaller investment opportunity set. Thus, many who consider the ESG framework to be *values* oriented argue that it is necessarily a constrained optimization problem and that ESG portfolios cannot be expected to outperform conventional portfolios (e.g., Geczy, Stambaugh, and Levin (2021)).

¹⁸ People also have a tendency to search for evidence that corresponds to their beliefs. See Alex Edmans' *think* London Business School contribution: <https://www.london.edu/think/why-truth-is-not-enough>.

In contrast, if the ESG investing approach arises from a *value* perspective, that is, a risk and return perspective, the underlying framework depends on the idea that ESG investing can result in better risk management or can identify return opportunities. This view suggests that expected returns should not be negatively affected by the approach and could even benefit from such an approach, resulting in lower risks or higher returns. For example, there could be less downside risk due to avoidance of ESG risks (e.g., Hoepner et al. (2022)) or there could be higher returns due to consumer demand and product differentiation (e.g., Albuquerque et al. (2019)). Other researchers find no significant costs associated with this type of investment approach (e.g., Humphrey and Tan (2014), Lindsay, Pruitt, and Schiller (2022)). Further, as noted above, survey evidence indicates that material subsets of both retail investors (e.g., Giglio et al. (2023)) and institutional investors (e.g., Krueger, Sautner, and Starks (2020)) believe that higher ESG investments will lead to larger returns.

Since the earliest ESG research (e.g., Hamilton, Jo, and Statman (1993) and Guerard (1997)), thousands of studies have examined the performance of ESG or SRI portfolios (or firms). Not surprisingly, conclusions vary as to whether CSR/SRI/ESG attributes add to corporate value and the risk premiums that can arise.¹⁹

The question I pose here is not whether ESG investing results in higher or lower returns or risk, but rather whether we have been asking the pertinent questions about ESG portfolios and investment performance. In particular, can we reasonably expect to answer the question of whether ESG can deliver superior performance when it is muddled by the vast array of investment strategies that come under the ESG umbrella? An inherent limitation in comparing portfolio results across time and studies is that the samples consist of an amalgam of funds with different types of objectives and approaches. Even a cursory examination of ESG mutual funds or ETFs highlights fundamental differences in investment strategies across the funds, which can be large. For example, some fund objectives appear to have a *values* orientation such as those whose objectives have a sole focus on social justice, sustainable development goals (SDGs), the circular economy, and negative screening according to Shariah or Catholic values, while other strategies appear to have a *value* orientation such as integrating ESG into the investment process or an ESG positive tilt. Yet, other strategies could exhibit both orientations, for example, renewables or transitioning to an energy future. Even if narrowed by broad themes, there still exist many differences in ESG funds, including differences in distribution systems

¹⁹ See, for example, Statman and Glushkov (2009, 2016), Edmans (2011), Humphrey, Lee, and Shen (2012), Krueger (2015), Khan, Serafeim, and Yoon (2016), Lins, Servaes, and Tamayo (2017), Bolton and Kacperczyk (2021a, 2022a), Lo and Zhang (2021), Lindsay, Pruitt, and Schiller (2022), Bansal, Wu, and Yaron (2022), Hwang, Titman, and Wang (2022), among many others. See, for example, Friede, Busch, and Bassen (2015) and Whelan et al. (2021) for meta-analyses. Related to the literature on performance is the literature on sin stocks and whether their exclusion affects portfolios. I discuss this in the section on divestment and exclusion (Section IV.B.)

and across benchmarks.²⁰ Thus, an inherent problem exists in many empirical studies of ESG fund performance because the samples consist of an amalgam of funds with different types of objectives and underlying approaches, leading to no basis to expect similar performance. This begs the question as to how it can be logical to combine such funds into one sample for testing purposes.

Similarly, empirical studies that focus on ESG or SRI funds typically do not differentiate between funds that primarily make decisions based on *values*, that is, nonpecuniary preferences, versus *value*, that is, risk factors. This mixing of funds with different objectives complicates our understanding of the effects of ESG investment decisions, making it more difficult to assess those effects financially, or to assess the effects that the portfolio firms have on society. Even if a study is limited to *values* funds, that is, those funds that focus exclusively on nonpecuniary considerations, heterogeneity of shareholder preferences in such funds (e.g., a preference to address issues pertaining to animal rights, child labor, gender diversity, or climate change) raises the question as to whether it makes sense to put all of these portfolios in the same bucket for comparison with conventional funds. There exist vast differences between omitting sin stocks or pharmaceutical stocks because of religious values and omitting fossil fuels because of nonpecuniary or financial concerns about climate change.

I emphasize that I am not criticizing the important work that has been conducted on this topic to date, rather given the broad array of ESG fund types, I am drawing attention to the opportunity to greatly improve our understanding by conducting more in-depth analyses that consider the differences in both objectives and investment approaches.

B. Firm Outcomes

Another area of confusion about the meaning of ESG is in the differences between assessing a company's processes and the outcomes of those processes. Many investors, particularly *value* investors who employ ESG factors to understand firm risk, are often most interested in business processes, particularly in terms of firms' risk management processes. These are the investors for which most ESG rating services are designed, as the rating services primarily examine firm risks associated with ESG activities.

Other investors, particularly *values* investors, are most interested in the effects of firms' business decisions on the environment and the firms' communities. For example, shareholders focused on outcomes tend to be concerned about negative environmental and social externalities, which can result in eco-

²⁰ An example of a paper that takes different benchmarks into account is Baker, Egan, and Sarkar (2022).

conomic damages to communities and society.^{21,22} Impact investors are *values* investors who tend to be most interested in outcomes.

Values investors focused on the consequences of business operations often want their portfolio companies to adhere to the United Nations SDGs (although many SDGs do not have investable elements). A prime example of outcomes that investors have concerns about is the effect of businesses on biodiversity. The UN Biodiversity Conference (COP 15) recently addressed this issue with an agreement on December 19, 2022, in which 188 countries pledged to adopt the Kunming-Montreal Global Biodiversity Framework (GBF). The GBF has goals of addressing biodiversity loss, restoring ecosystems, and protecting indigenous rights.²³ The 2030 goals include requiring “large and transnational companies and financial institutions to monitor, assess, and transparently disclose their risks, dependencies and impacts on biodiversity through their operations, supply and value chains and portfolios.”²⁴ Guidance on how to disclose biodiversity risk already exists with the Task Force for Nature-related Financial Disclosures (TNFD).²⁵ As finance researchers, we can provide insights into how this risk is priced by financial markets. As Karolyi and Tobin-de la Puente (2023) point out, we need research that helps us better understand these risks, how they might be priced, and how the financing of biodiversity goals can be achieved.²⁶ Again the question can be better understood by differentiating between the *value* and *values* perspectives.

C. ESG Issues beyond Equity Asset Classes

Financial economics research that focuses on ESG issues tends to do so in regard to equities, but is increasingly considering those issues in regard to other asset classes such as fixed income and real estate. For example, prior studies find relationships between a firm’s environmental or social qualities and the pricing and risk of its debt (e.g., Chava (2014), Bae et al. (2019), Kacperczyk and Peydro (2022), Seltzer, Starks, and Zhu (2022)).²⁷ For fixed income assets, whether a firm’s negative externalities create more tail risk for investors in these assets is an open question, particularly since Bai, Bali, and

²¹ Humphrey et al. (2022) provide evidence that investors are affected more by negative externalities than positive externalities.

²² This view of the double bottom line is also related to extensive work in accounting, economics, finance, and management on the topic and on additional issues that can arise such as conflicts of interest. See, for example, Christensen, Hail, and Leuz (2021), and Karlan, Osman, and Zinman (2021).

²³ See <https://www.unep.org/news-and-stories/story/cop15-ends-landmark-biodiversity-agreement#:~:text=The%20United%20Nations%20Biodiversity%20Conference,on%20nature%20through%20to%202030.>

²⁴ See <https://www.cbd.int/convention/>.

²⁵ See <https://tnfd.global/>.

²⁶ See also the recent work on biodiversity by Flammer, Giroux, and Heal (2023) and Garel et al. (2023).

²⁷ Houston and Shan (2022) provide evidence that a firm’s banking relationships can promote better ESG performance for its borrowers.

Wen (2019) find that in the cross section, downside risk is the strongest predictor of future bond returns. Seltzer, Starks, and Zhu (2022) document that firms with poor environmental performance, or high carbon emissions, that are affected by heightened expected regulatory risk face downside risk effects. Ilhan, Sautner, and Vilkov (2021) show that for equities, the cost of option protection against downside tail risk is larger for firms with greater carbon intensity. Better understanding the effects of downside risks from other ESG issues would be valuable.

Indeed, much work remains to be done on the ESG issues and asset classes beyond equities, particularly with regard to risk and pricing. Examining differences between *value* and *values* investors should help with this. For example, innovative types of bonds related to ESG require more scrutiny. Although there exists a growing body of work on GSSS (green, social, sustainability, and sustainability-linked) bonds, these are such new instruments that the future will tell us much more about how markets treat such bonds. Again, some investors prefer these bonds because they approach the market from a *value* perspective, while other investors view the bonds from a *values* perspective. Examination of green corporate and municipal bonds has enhanced our knowledge, but it is still limited and as the bond category matures, investor reactions and issuer decisions may vary.²⁸ Given the increasing issuance of sovereign green bonds and evidence on the existence of a greenium versus a green spread for these bonds (e.g., D'Amico, Klausman, and Pancost (2022), Pastor, Stambaugh, and Taylor (2022)), it would help to further improve our understanding of how the *values* versus *value* perspective affects the pricing of GSSS bonds, whether issued by corporations or by sovereigns.

Does the shift from public markets to private markets have implications for firms' ESG activities? Arguments have been made that portfolio and financial institution decarbonization efforts will lead more companies with problematic carbon emissions to move to private markets. However, recent research indicates that private companies are associated with less pollution (Shive and Forster (2020)). In addition, the results in Bellon (2022) suggest that the answer is not straightforward as private equity governance and firm liability become important in the determination.

D. The Framing of the ESG Issues

Does it make sense to talk about ESG issues as if they represent a consolidation of similar issues? While the term ESG is efficient terminology, investor preferences are unlikely to link these issues together (witness the different types of designated ESG funds, many of which focus only on particular environmental, social, or governance issues). In addition, company managers do not treat each issue equally, as can be discerned from their communications to investors, customers, and employees. Some companies' disparate focus is reflected in ESG rating service providers' scores as shown in Table I, which

²⁸ See, for example, Tang and Zhang (2020), Flammer (2021), Pastor, Stambaugh, and Taylor (2022), D'Amico, Klausman, and Pancost (2022), and Baker et al. (2022).

Table I
Correlations across Companies' Environmental, Social, and Governance (ESG) Scores

This table reports pairwise correlations between individual companies' ESG scores. Panel A reports the correlations using Sustainalytics scores from 2013 to 2017. Panel B reports the correlations using S&P Global scores from 2013 to 2017, and Panel C reports the correlations using S&P Global scores from 2018 to 2022.

Panel A. Correlations across E, S, and G scores using Sustainalytics Scores from 2013 to 2017			
	Environmental Score	Social Score	Governance Score
Environmental Score	1.00		
Social Score	0.544	1.00	
Governance Score	0.483	0.408	1.00

Panel B. Correlations across E, S, and G scores using S&P Global Scores from 2013 to 2017			
	Environmental Score	Social Score	Governance Score
Environmental Score	1.00		
Social Score	0.818	1.00	
Governance Score	0.669	0.688	1.00

Panel C. Correlations across E, S, and G scores using S&P Global Scores from 2018 to 2022			
	Environmental Score	Social Score	Governance Score
Environmental Score	1.00		
Social Score	0.876	1.00	
Governance Score	0.749	0.819	1.00

reports pairwise correlations between individual companies' ESG scores.²⁹ Using Sustainalytics score data from 2009 to 2017, the pairwise correlations all lie below 55%.³⁰ In comparison, the S&P Global score data for the same period show somewhat higher correlations in Panel B, but still indicate differences in how companies may treat the ESG issues. More recent data from S&P Global for the 2018 to 2022 period in Panel C suggest that the variation within firms

²⁹ It is possible that the low correlations arise from difficulties in measuring the different ESG aspects of a company, particularly for earlier periods, or that rating service providers view the aspects differently.

³⁰ I employ scores between 2009 and 2017 because Sustainalytics changed their rating methodology in 2018 and they no longer provide a combined ESG score. They also no longer provide academic researchers the aggregated individual environmental, social, or governance risk ratings for a firm, although as of this time, the current measures are available on Yahoo.com.

in addressing of ESG activities has declined. Notably, companies' treatment of environmental and social issues is much more closely correlated across all of the measurements. We need to better understand the implications of these correlation differences. For example, what do such differences imply for our understanding of how companies (and ultimately investors) treat environmental and social issues as perhaps distinct from governance issues? Similarly, we need to better understand how investors motivated by *value* differ from investors motivated by *values* in considering the importance of individual ESG issues.

Although a large literature on corporate governance has developed over many years and research on environmental issues, particularly climate finance, is on the rise, the tradition among academics and the media is to focus on aggregate ESG. But the ESG terminology arose because of a report from a meeting requested by Kofi Annan.³¹ Is there a reason to continue using this terminology? Based on both a *value* and *values* perspective, going forward, it may be preferable to consider these as separate risk factors or preference points.^{32,33}

III. *Value, Values, and Environmental Issues, Including Climate Risk*

Given the growing interest in the academic literature, this entire address could have focused on environmental issues and in particular, on climate risk. Note that climate risk is an ESG risk for companies and their investors.³⁴ In addition, as discussed above, there exist both *value* and *values* preferences around climate issues. We still need a better understanding of how different types of investors' and managers' decisions are influenced by pecuniary and nonpecuniary concerns.

As has been pointed out previously (e.g., Krueger, Sautner, and Starks (2020)), climate risk is difficult to assess, primarily due to insufficient disclosure. It is therefore difficult to price and to hedge because it is systematic and it is difficult to find suitable instruments to hedge climate risk. Moreover, since climate risk is a major focus for both policy makers and activists, the regulatory and reputational risks can be significant.

With regard to climate finance research, only a few papers existed prior to 2017. Thanks to a grant from the Norges Bank Investment Management's Norwegian Finance Initiative as well as other financial support, Harrison Hong,

³¹ See https://www.unepfi.org/fileadmin/events/2004/stocks/who_cares_wins_global_compact_2004.pdf.

³² Moreover, when people talk about sustainable finance, they often are referring to the environmental aspect alone, but as pointed out earlier, others think about sustainable finance as including not only ESG, but also economic sustainability. Without a business being economically sustainable, the other issues will not come into play in the first place.

³³ Indeed, many, perhaps most, *value* and *values* investors do not employ the combined ESG score but rather are more interested in the individual components such as carbon footprint, animal rights, or governance quality. Moreover, many practitioners that incorporate the individual ESG risk factors into their analysis do not employ the third-party ESG quantitative scores at all, rather they consider the underlying analysis provided by the ratings services.

³⁴ Beyond constituting an obvious environmental risk, climate risk is also a social risk (e.g., environmental injustice) and a governance risk (e.g., climate risk management oversight).

Andrew Karolyi, and Jose Scheinkman put out a call for proposals on climate finance for two conferences and a special issue of the *Review of Financial Studies* that was published in March 2020. In the last few years, academic work related to this topic has grown significantly. Indeed, Gasparini and Tufano (2023) identify over 500 papers on the topic.³⁵ Yet, it seems like we have only gotten to the tip of the iceberg (with icebergs themselves at risk). For example, although excellent work exists on the pricing and effects of carbon emissions as well as on hedging (e.g., Andersson, Bolton, and Samama (2016), Engle et al. (2020), Bolton and Kacperczyk (2021a, 2022a, 2022b), Bolton, Kacperczyk, and Samama (2022)), there is still much we do not understand about how markets treat this risk and how corporations manage it. We need more research on investors' and managers' views toward different types of climate risks (physical, transitional [policy, regulatory, liability, technological], reputational) along with differences across their time horizons and the differences between risk and uncertainty with regard to climate change. We also need a better understanding of the extent to which the climate-related decisions of different investor groups and managers are due to financial concerns versus nonpecuniary preferences.

In particular, we need more work to better understand the extent to which firm decisions are driven by climate risk management (*value*) versus the preferences of the firm's leadership (*values*). For example, Sautner et al. (2022) find that banks charge a lower interest rate on loans to firms with more EU taxonomy-aligned transitional revenue, with two channels explaining their results: climate risk management on the part of the banks and the banks' "green" preferences. We also need to better understand the behavioral finance effects and their consequences. For example, Anderson and Robinson (2021) find that extreme beliefs about future climate disasters can affect individuals' expectations and investment choices.

To understand how investors and managers react to changes in climate risk and other ESG issues, we also need to improve our understanding of the motivations for and effects of disclosure. A nascent line of research exists on this topic (e.g., Christensen, Hail, and Leuz (2021), Goldstein et al. (2022), Ilhan et al. (2023), Krueger et al. (2023), Bolton and Kacperczyk (2021b), but much more research needs to be done. As Christensen, Hail, and Leuz (2021) point out, these types of disclosures can target a wider audience and can have important externality benefits beyond the firm. In particular, for some the goal of disclosure on ESG issues is to gain better knowledge about the firm through an ESG lens, while for others the goal is to drive wider change through the disclosure regime. We therefore need to consider the differences between the importance of these disclosures to *value* and *values* investors.

There also exist differences among *value* investors in how they conceptualize climate and other ESG risks. For example, some see ESG risks as fundamental risk factors and want to avoid or mitigate such risks as well as understand how they are priced. These investors would be particularly interested in improved

³⁵ See also Hong, Karolyi, and Scheinkman (2020), Matos (2020), Giglio, Kelly, and Stroebe (2021), and Stroebe and Wurgler (2021) for overviews of climate finance work.

ESG disclosure and regulation. Other *value* investors may be more concerned about the regulatory risks that can arise from ESG issues, how to reduce the firm's exposure to these risks, and therefore would be interested in enforcing ESG compliance. Still other investors may be interested in how firms can avoid the additional regulatory requirements since they view them as too onerous.

IV. *Value, Values, and the Role of Owners: Voice versus Exit*

A. *Shareholder Activism on ESG Issues*

For many years, shareholders have pressed firms to make ESG changes through public and private engagement. One such approach has been through shareholder proposals. The early shareholder proposals related to environmental and social issues argued that shareholders should vote in favor of the proposal based on ethical, moral, and/or social reasons. But the proponents' arguments shifted over time as they began to argue that shareholders should vote in favor of the proposal based on arguments that an economic rationale exists because CSR can affect company performance (Starks (2009)).³⁶

Important studies exist on the role of institutional investor engagement, primarily on governance issues and the choice of using voice or exit (e.g., Gillan and Starks (2000), Admati and Pfleiderer (2009), Becht et al. (2009), Edmans (2009), McCahery, Sautner, and Starks (2016), Becht et al. (2017)). Recent studies focus in particular on engagement and shareholder voting on environmental and social issues.³⁷ These studies provide evidence that shareholder activism and firm engagement can affect management decisions with managers changing the firm's environmental and social policies as a result of the shareholder proposals and direct engagement.

Motivations for shareholder activism and firm engagement also differ across *value* and *values* proponents. Motivations for some activists arise from a *value* orientation (such as many hedge funds; see Akey and Appel (2020), Naaraayanan, Sachdeva, and Sharma (2021), and Hoepner et al. (2022)). Other shareholder activists coordinate through religious organizations such as the Interfaith Center on Corporate Responsibility to address their *values* concerns. We should expect differences in engagement tactics and results depending on the *value* versus *values* orientation of the shareholder, and our theories and empirical tests should reflect those differences. We need more analysis on the differences across the *value* versus *values* motivations of both shareholder proposal sponsors and voters.³⁸

³⁶ See also Campbell, Gillan, and Niden (1999) and Tkac (2006).

³⁷ See, for example, Dimson, Karakas, and Li (2015, 2021), Flammer, Toffel, and Viswanathan (2021), Hoepner et al. (2022), Naaraayanan, Sachdeva, and Sharma (2021), Akey and Appel (2020), Chen, Dong, and Lin (2020), and He, Kahraman, and Lowry (2023).

³⁸ For example, Bolton et al. (2020) estimate investor preferences from their proxy voting and show a difference between voting based on preferences and voting by "money-conscious" investors. Regarding shareholder voting by ESG funds, Lowry, Wang, and Wei (2023) consider differences across holding periods, chosen risk exposure, and discretionary voting.

B. Exclusion/Divestment

An important aspect of climate risk as well as other ESG issues is the question of exclusion and divestment. This again comes back to the question of *value* versus *values*. A *value* investor may have concerns about the financial implications of a firm or industry causing an investment to be too risky, with the potential for the assets to become stranded. Alternatively, an investment fund such as a sovereign wealth fund may have concerns about its portfolio's diversification from its source of funds. Turning to *values* investors' considerations, these investors may be unwilling to provide capital to, or receive profits from, companies that contribute to climate change or that are considered to do social harm through their products or actions. Yet, other *values* investors may divest in an effort to force the company to change its business model to eliminate or at least mitigate negative externalities. These investors argue that divesting puts pressure on the company's cost of capital, driving it higher, and thus, gives managers incentives to take corrective actions.

Research on the costs of exclusion and divestment has provided mixed results. Early work on so-called sin stocks finds that they earn risk premiums because of investor avoidance (e.g., Hong and Kacperczyk (2009), Statman and Glushkov (2009)), which of course implies that there is a cost to investors that exclude these stocks.³⁹ Similarly, Bessembinder (2016) provides some evidence that exclusion of fossil fuel companies can be costly to pension plans and endowments. Beyond examining the financial costs (or benefits) of exclusion or divestment from the investor's perspective, we also must examine whether divestment can result in lasting or meaningful change. There is some question about the potential impact of this approach because an investor cannot directly engage the company or vote on proxy proposals after divestment. Extant empirical research calculates the costs of exclusion on investors or beneficiaries to be relatively high.⁴⁰ Moreover, Teoh, Welch, and Wazzan (1999) find little discernible effect on firm values from South African divestments. On the other hand, Gantchev, Giannetti, and Li (2022a) provide evidence that under certain conditions, such as the presence of environmentally and socially conscious institutional investors, exclusion may be effective.

In theoretical work, Davies and van Wesep (2018) cast doubt on the efficacy of divestment based on the design of managerial compensation contracts. The idea is that while divestment campaigns may affect stock return performance in the short run, managerial compensation structures do not depend on short-run performance, rather they are designed to reward managers over the long term, and hence managerial incentives are not likely to be affected by divestment campaigns. Edmans, Levit, and Schneemeier (2022) also consider managerial incentives and show theoretically that although excluding firms can minimize negative externalities for a portfolio, there exist no incentives

³⁹ See also Pedersen, Fitzgibbons, and Pomorski (2021), Lo and Zhang (2021), Eccles, Rajgopal, and Xie (2022), and Zerbib (2022).

⁴⁰ For an earlier view on these issues, see Skancke et al. (2014).

for firm management to pursue corrective changes because the firm will be excluded regardless. Their model indicates that portfolio tilting would be a better approach because it would allow investors to engage the firm's management in taking corrective actions. Berk and van Binsbergen (2022) argue that divestment's effect on a firm's cost of capital will be too low to make a difference. They estimate that to effect a more than 1% change in a firm's cost of capital would require that the *values* investors trying to bring about this effect make up more than 80% of all investable wealth.⁴¹

However, as pointed out by Becht, Pajuste, and Toniolo (2022), perhaps the goals of divestment movements need to be considered as these movements may be designed to exert social pressure for change. Statman (2000) argues that investment actions such as divestments are more likely to effect change by serving as banners for subsequent political actions rather than through the action itself.

A number of institutional investors (often public pension funds, endowments, and foundations) have announced plans to divest from fossil fuel companies. In addition, empirical studies indicate that some divestment is already occurring as institutional investors are increasingly excluding or reducing ownership in companies with high carbon emissions. For example, Atta-Darkua et al. (2022) show that although institutional investors' holdings of public equity grew from 43% to 53% over the 2005 to 2019 period, those holdings account for only 9% of public equity's carbon emissions throughout that period. Importantly, the authors provide evidence that while these institutional investors are engaging firms on their carbon emissions, their portfolios are being decarbonized primarily due to portfolio reweighting rather than through shareholder engagement.

What has not been established by the prior studies on divestment are differences between the motivations of *value* and *values* investors in the exclusion decision. While studies on the limitations of divestment may make sense to a *value* investor, it is not clear that a *values* investor who wants to exclude stocks because of a desire for noncomplicity will be moved by such arguments. If *values* investors increase in numbers relative to *value* investors, then we need to understand how that will affect financial markets. Pastor, Stambaugh, and Taylor (2021) provide some theoretical guidance on this question.

C. Value and Values: Politics, Regulation, ESG Considerations and Population Demographics

ESG has become a political issue with some politicians stating that they are anti-ESG.⁴² Given that the meaning of ESG is not clear, it is even more difficult to understand what is meant by the term, anti-ESG. Using the *value* versus

⁴¹ Broccardo, Hart, and Zingales (2022) argue that divestment's effectiveness depends on the motivations of the majority of the firm's shareholders.

⁴² There exists research on political differences between founders/CEOs/directors and a firm's social responsibility (Di Giuli and Kostovetsky (2014)), differences across mutual fund managers in their holdings of socially responsible firms and their political affiliations (Hong and Kostovetsky

values paradigm, there are two implications. The first is that those who are anti-ESG believe investors should not invest according to their values, which implies that the anti-ESG advocates are against allowing investors to select investments based on their personal preferences, including those who invest according to religious values, such as Catholic or Shariah values. This raises the question as to whether *values* investors should be restricted from investing their own money (including their defined contribution retirement funds) according to their preferences. As discussed earlier, Baker, Egan, and Sarkar (2022) and Barber, Morse, and Yasuda (2021) provide evidence that some people are willing to give up returns to invest according to their preferences.

The second implication is that anti-ESG advocates are stating that they are against *value* investors using information about firms' ESG profiles to assess firms' risks and returns. The further implication in this case is that pension fund sponsors should not be allowed to follow their fiduciary duty because of a requirement that they exclude consideration of potentially relevant risks with financial implications.

Although we have a responsibility to inform *values* investors of the costs of divesting certain industry sectors or companies, should finance researchers or government officials tell *values* investors who do not want to be complicit in their investing that they should not invest according to their preferences if they are willing to pay? What if offering ESG funds in defined contribution plans actually results in participants saving more money toward their retirement? I have a colleague who told me that his mother had always refused to invest in equity mutual funds until she had the opportunity to invest in ESG mutual funds.

It should also be noted that the costs of imposing values on financial market participants can arise from different political stances.⁴³ Legislation increasingly either requires divestments such as in California and Maine or takes the opposite stance and not only forbids ESG from being employed in investments, but also boycotts investment firms from doing business with state governments. Such positions can have costs. For instance, beyond the potential costs of divestment discussed above, Garrett and Ivanov (2023) provide evidence that Texas legislation resulting in the banning of some of the largest municipal bond underwriters from doing business in the state has had a significant cost on the issuers of municipal bonds, a cost that is borne by Texas taxpayers.

Another issue arises from the question of *values* investors and their preferences. Preferences can move markets, and if they are long-term preferences, then they can affect asset allocations. We need to understand how *values* investors' preferences are changing, which potentially requires a better under-

(2012)), and corporate donations to legislators to try to lessen environmental compliance costs (Fich and Xu (2023)). See also Edmans (2022) for discussion of the politicization of ESG.

⁴³ The question of whether and how regulation can combat climate change is important and requires more research. A number of research studies consider the effects of regulatory requirements on climate change. See, for example, Wu et al. (2022).

standing of the demographics of the investment population and their preferences. As Roy (2022) argues, “...demographic heterogeneity and behavioral characteristics play a significant role in determining micro-differences underlying macro-aggregates and, consequently, prices in cross-section and over time” (p. 97)

Related, we need more research on whether and how demographics and future demographic shifts affect corporate focus on ESG issues. Similar to the evidence on WTP for certain types of investments discussed earlier, empirical studies have provided evidence that consumers are increasingly selecting sustainably marketed products and those products are growing faster than conventional products (Whelan and Kronthal-Sacco (2019)). Prior work also suggests that employees have strong preferences for their employers’ sustainability profile. Krueger, Metzger, and Wu (2022), for instance, find that Swedish workers are willing to work for less pay for a company in a sustainable sector.⁴⁴

V. Social and Governance Issues

In this section, I briefly discuss social and governance issues individually. The first challenge arises because social issues are not well defined and the meaning often differs not only between *value* and *values* investors, but even within *value* and *values* investor communities. Moreover, social issues are more multifaceted than environmental issues for both *value* and *values* investors and views on social issues can differ strongly across individuals, that is, on nearly any social issue of disagreement, both sides believe they are on the “right” side. This has real implications as companies find themselves embroiled in controversies related to social issues. As finance researchers, we need to be precise in our definitions and in whether a particular social issue is being considered from a *value* or *values* perspective.

With regard to governance, there continues to exist disagreement on what constitutes good corporate governance. According to Berg, Koelbel, and Rigobon (2022), the average correlation across the ESG ratings services for governance in their sample is around 30%, which is much lower than across the environmental or social ratings. This result suggests that governance is difficult to measure or there exists substantial disagreement about what constitutes good governance. Moreover, debate surrounds the question of the appropriate objective function for a firm.⁴⁵

Corporate boards are increasingly paying attention to ESG issues as seen by changes in committee structures and the fact that some boards are incorpo-

⁴⁴ This could also extend to employees in other countries as Briscoe-Tran (2023) employs employees’ reviews posted on Glassdoor.com and finds that employees have access to information useful for assessing firms’ ESG practices.

⁴⁵ There exists an active debate on the related question of stakeholder capitalism versus shareholder capitalism. This topic is well discussed in other work (e.g., Hart and Zingales (2017), Bebchuk and Tallarita (2020), Edmans (2020), Karpoff (2021), Starks (2021), Graham (2022)), and thus I do not discuss it here.

rating ESG metrics into executive compensation. This is the case even though the metrics are not yet “mature” and thus, not surprisingly, the inclusion of ESG metrics in executive compensation is also being questioned (e.g., Edmans (2022), Bebchuk and Tallarita (2022)). However, evidence suggests that overall, firms that use environmental and social metrics in their executive compensation contracts have better business performance as well as environmental and social performance (Flammer, Hong, and Minor (2021)). If one examines the individual firm ESG metrics employed in compensation packages, they usually are not a combination of metrics but tend to consist of a focus on the separate ESG elements. More research in this area is needed as additional ESG metrics are increasingly adopted.

Despite the extensive body of research on corporate governance issues, there still exists much that we can learn about governance. For example, we do not understand how and how much racial, ethnic, and gender diversity contributes to corporate leadership, including the board of directors, and firm performance. Nor do we fully understand the role of institutional investors, including hedge funds, in a firm’s corporate governance.⁴⁶ We could shed light on this question by considering the *value* and *values* perspectives and how they affect the social and governance aspects of a firm. For example, companies have faced pressure for some time to increase diversity on their boards, including skill diversity, gender diversity, and racial and ethnic diversity. The rationales underlying the calls for diversity have varied, ranging from *value* to *values* justifications. Questions that need to be addressed include whether boards primarily consider skills, gender, or both (e.g., Kim and Starks (2016)), whether the skills more dominated by women exist on boards prior to the appointment of a woman with that skill, whether women directors bring new CSR activities to firms, how board heterogeneity impacts firm value and performance, what are the possible channels for board heterogeneity to affect cash flows and risk, are they associated with the advisory role of the board or the monitoring role of the board, and are the advisory and monitoring roles with respect to board heterogeneity substitutes or complements? We have made strides in these areas, but more work needs to be done.⁴⁷ Perhaps the most important question is whether one can really have good environmental and social performance without good governance, that is, without good corporate governance, how can management make the appropriate decisions on environmental and social issues?

VI. Conclusions

What ESG investing means depends on the context. ESG *value* implies that the ESG activities can be financially important, particularly for long-term in-

⁴⁶ See, for example, McCahery, Sautner, and Starks (2016), Hartzell and Starks (2003), Kedia, Starks, and Wang (2021), and Brav, Jiang, and Li (2022).

⁴⁷ See, for example, Carter, Simkins, and Simpson (2003), Adams and Ferreira (2009), Kim and Starks (2016), Adams (2017), Giannetti and Zhou (2019), Field, Souther, and Yore (2020), Giannetti and Wang (2023), Gormley et al. (2022), and Eckbo, Nygaard, and Thorburn (2022) among many others.

vestors. This value can come through risk management and return opportunities, including shareholder engagement activities. In contrast, the term *ESG values* relates to nonpecuniary factors that are important.

These differences have important implications. For example, considerations about what ESG investing means and interpretations of ESG performance evidence depend on which context is important to the investors. ESG investing approaches can differ greatly based on whether the motivation is based on *ESG value*, *ESG values*, or both.

Our understanding of the complex relations between ESG issues and financial markets is clouded by these dual motives—*value* versus *values*. As financial economics researchers, there is an incredible opportunity to meaningfully contribute to this critical topic, to society, and to public policy by delving deeper into understanding how *value* and *values* orientations and their interactions impact the relations among investors, companies, and societies.

REFERENCES

- Adams, Renee B., 2017, Boards and the directors who sit on them, in Benjamin E. Hermalin and Michael S. Weisbach, eds.: *The Handbook of the Economics of Corporate Governance* Volume 1, (North Holland, Amsterdam).
- Adams, Renee B., and Daniel Ferreira, 2009, Women in the boardroom and their impact on governance and performance, *Journal of Financial Economics* 94, 291–309.
- Admati, Anat, and Paul Pfleiderer, 2009, The “Wall Street Walk” and shareholder activism: Exit as a form of voice, *Review of Financial Studies* 22, 2245–2485.
- Akey, Pat, and Ian Appel, 2020, Environmental externalities of hedge funds, Working paper, University of Toronto.
- Albuquerque, Rui, Yrjo Koskinen, and Chendi Zhang, 2019, Corporate social responsibility and firm risk: Theory and empirical evidence, *Management Science* 65, 4451–4469.
- Ammann, Manuel, Christopher Bauer, Sebastian Fischer, and Philipp Müller, 2018, The impact of the Morningstar Sustainability Rating on mutual fund flows, *European Financial Management* 25, 520–553.
- Anderson, Anders, and David T. Robinson, 2021, Climate fears and the demand for green investment, Swedish House of Finance Research Paper 19-14.
- Andersson, Mats, Patrick Bolton, and Frederic Samama, 2016, Hedging climate risk, *Financial Analysts Journal* 72, 13–32.
- Atta-Darkua, Vaska, Simon Glossner, Philipp Krueger, and Pedro Matos, 2022, Decarbonizing institutional investor portfolios, Working paper, University of Virginia.
- Bae, Kee-Hong, Sadok El Ghoul, Omrane Guedhami, Chuck Y. Kwok, and Ying Zheng, 2019, Does corporate social responsibility reduce the costs of high leverage? Evidence from capital structure and product market interactions, *Journal of Banking and Finance* 100, 135–150.
- Bai, Jennie, Turan G. Bali, and Quan Wen, 2019, Common risk factors in the cross-section of corporate bond returns, *Journal of Financial Economics* 131, 619–642.
- Baker, Malcolm, Daniel Bergstresser, George Serafeim, and Jeffrey Wurgler, 2022, The pricing and ownership of U.S. green bonds, *Annual Review of Financial Economics* 14, 415–437.
- Baker, Malcolm, Mark L. Egan, and Suproteem K. Sarkar, 2022, How do investors value ESG? NBER Working Paper 30708.
- Baker, Steven D., Burton Hollifield, and Emilio Osambela, 2022, Asset prices and portfolios with externalities, *Review of Finance* 26, 1433–1468.
- Bansal, Ravi, Di (Andrew) Wu, and Amir Yaron, 2022, Socially responsible investing in good and bad times, *Review of Financial Studies* 35, 2067–2099.

- Barber, Brad M., Adair Morse, and Ayako Yasuda, 2021, Impact investing, *Journal of Financial Economics* 139, 162–185.
- Baron, David P., 2007, Corporate social responsibility and social entrepreneurship, *Journal of Economics & Management Strategy* 16, 683–717.
- Baron, David P., 2008, Managerial contracting and corporate social responsibility, *Journal of Public Economics* 92, 268–288.
- Bauer, Rob, Tobias Ruof, and Paul Smeets, 2021, Get real! Individuals prefer more sustainable investments, *Review of Financial Studies* 34, 3976–4043.
- Bebchuk, Lucian, and Roberto Tallarita, 2020, The illusory promise of stakeholder governance, *Cornell Law Review* 106, 91–178.
- Bebchuk, Lucian, and Roberto Tallarita, 2022, The perils and questionable promise of ESG-based compensation, *Journal of Corporation Law* 48, 38–75.
- Becht, Marco, Julian Franks, Colin Mayer, and Stefano Rossi, 2009, Returns to shareholder activism: Evidence from a clinical study of the Hermes UK Focus Fund, *Review of Financial Studies* 22, 3093–3129.
- Becht, Marco, Julian Franks, Jeremy Grant, and Hannes F. Wagner, 2017, Returns to hedge fund activism: An international study, *Review of Financial Studies* 30, 2933–2971.
- Becht, Marco, Anete Pajuste, and Anna Toniolo, 2022, Voice through divestment, ECGI Working Paper 900/2023.
- Bellon, Aymeric, 2022, Does private equity ownership make firms cleaner? The role of environmental liability risks, Working paper, University of North Carolina.
- Benabou, Roland, and Jean Tirole, 2010, Individual and corporate social responsibility, *Economica* 77, 1–19.
- Bennett, James A., Richard W. Sias, and Laura T. Starks, 2003, Greener pastures and the impact of dynamic institutional preferences, *Review of Financial Studies* 16, 1203–1238.
- Benson, Karen L., and Jacquelyn E. Humphrey, 2008, Socially responsible investment funds: Investor reaction to current and past returns, *Journal of Banking and Finance* 32, 1850–1859.
- Berg, Florian, Julian F. Koelbel, Anna Pavlova, and Roberto Rigobon, 2021, ESG confusion and stock returns: Tackling the problem of noise. Working paper, MIT.
- Berg, Florian, Julian F. Koelbel, and Roberto Rigobon, 2022, Aggregate confusion: The divergence of ESG ratings. *Review of Finance* 26, 1315–1344.
- Berk, Jonathan, and Jules H. van Binsbergen, 2022, The impact of impact investing, Working paper, Stanford University.
- Bessembinder, Hendrik, 2016, Frictional costs of fossil fuel divestment, Working paper, University of Utah.
- Bialkowski, Jędrzej, and Laura T. Starks, 2018, SRI funds: Investor demand, exogenous shocks and ESG profiles, Working paper, University of Canterbury.
- Bialkowski, Jędrzej, Laura T. Starks, and Moritz Wagner, 2022, Cultural values and cross-country differences in responsible investing sectors, Working paper, University of Canterbury.
- Bollen, Nicholas P.B., 2007, Mutual fund attributes and investor behavior, *Journal of Financial and Quantitative Analysis* 42, 683–708.
- Bolton, Patrick, and Marcin Kacperczyk, 2021a, Do investors care about carbon risk? *Journal of Financial Economics* 142, 517–549.
- Bolton, Patrick, and Marcin Kacperczyk, 2021b, Carbon disclosure and the cost of capital, Working paper, Imperial College London.
- Bolton, Patrick, and Marcin Kacperczyk, 2022a, Global pricing of carbon-transition risk, *Journal of Finance* (forthcoming).
- Bolton, Patrick, and Marcin Kacperczyk, 2022b, Firm commitments, Working paper, Imperial College London.
- Bolton, Patrick, Marcin Kacperczyk, and Frederic Samama, 2022, Net-zero carbon portfolio alignment, *Financial Analysts Journal* 78, 19–33.
- Bolton, Patrick, Tao Li, Enrichetta Ravina, and Howard Rosenthal, 2020, Investor ideology, *Journal of Financial Economics* 137, 320–352.
- Bonelli, Maxime, Marie Briere, and Francois Derrien, 2022, Altruism or self-interest? ESG and participation in employee share plans, Working paper, HEC Paris.

- Bonnefon, Jean-Francois, Augustin Landier, Parinitha R. Sastry, and David Thesmar, 2022, The moral preferences of investors: Experimental evidence, NBER Working paper 29647.
- Bose, Sudipta, Natasha Burns, Kristina Minnick, and Syed Shame, 2023, Climate-linked compensation, societal values, and climate change impact: International evidence, *Corporate Governance: An International Review* (forthcoming).
- Brav, Alon, Wei Jiang, and Rongchen Li, 2022, Governance by persuasion: Hedge fund activism and market-based shareholder influence, ECGI Working paper 797/2021.
- Briscoe-Tran, Hoa, 2023, Do employees have useful information about firms' ESG practices? ECGI Working paper 907/2023.
- Broccardo, Eleonora, Oliver Hart, and Luigi Zingales, 2022, Exit versus voice, *Journal of Political Economy* 130, 3101–3145.
- Broadback, Daniel, Nadja Guenster, and David Mezger, 2019, Altruism and egoism in investment decisions, *Review of Financial Economics* 37, 118–148.
- Broadback, Daniel, Nadja Guenster, Sebastien Pouget, and Ruichen Wang, 2022, The valuation of corporate social responsibility: A willingness-to-pay experiment, Working paper, University of Munster.
- Cai, Ye, Carrie H. Pan, and Meir Statman, 2016, Why do countries matter so much in corporate social performance? *Journal of Corporate Finance* 41, 591–609.
- Campbell, Cynthia J., Stuart L. Gillan, and Cathy M. Niden, 1999, Current perspectives on shareholder proposals: Lessons from the 1997 proxy season, *Financial Management* 28, 89–98.
- Carter, David A., Betty J. Simkins, and W. Gary Simpson, 2003, Corporate governance, board diversity and firm value, *Financial Review* 38, 33–53.
- Ceccarelli, Marco, Stefano Ramelli, and Alexander F. Wagner, 2022, Low-Carbon Mutual Funds. *Review of Finance* (forthcoming).
- Chava, Sudheer, 2014, Environmental externalities and cost of capital, *Management Science* 60, 2223–2247.
- Chen, Tao, Hui Dong and Chen Lin, 2020, Institutional shareholders and corporate social responsibility, *Journal of Financial Economics* 135, 483–504.
- Chowdhry, Bhagwan, Shaun William Davies, and Brian Waters, 2019, Investing for impact, *Review of Financial Studies* 32, 864–904.
- Christensen, Hans, Luzi Hail, and Christian Leuz, 2021, Mandatory CSR and sustainability reporting: Economic analysis and literature review, *Review of Accounting Studies* 26, 1176–1248.
- Daniel, Kent, Mark Grinblatt, Sheridan Titman, and Russ Wermers, 1997, Measuring mutual fund performance with characteristic-based benchmarks, *Journal of Finance* 52, 1035–1058.
- Davies, Shaun W., and Edward D. Van Wesep, 2018, The unintended consequences of divestment, *Journal of Financial Economics* 128, 558–575.
- D'Amico, Stefania, Johannes Klausmann, and N. Aaron Pancost, 2022, The benchmark greenium, Working paper, Federal Reserve Bank of Chicago.
- Di Giuli, Alberta, and Leonard Kostovetsky, 2014, Are red or blue companies more likely to go green? Politics and corporate social responsibility, *Journal of Financial Economics* 111, 158–180.
- Dimson, Elroy, Oguzhan Karakas, and Xi Li, 2015, Active ownership, *Review of Financial Studies* 28, 3225–3268.
- Dimson, Elroy, Oguzhan Karakas, and Xi Li, 2021, Coordinated engagements, ECGI Working Paper 721/2021.
- Doidge, Craig, Andrew Karolyi, and Rene Stulz, 2007, Why do countries matter so much for corporate governance? *Journal of Financial Economics* 86, 1–39.
- Dyck, Alexander, Karl V. Lins, Lukas Roth, and Hannes F. Wagner, 2019, Do institutional investors drive corporate social responsibility? International evidence, *Journal of Financial Economics* 131, 693–714.
- Eccles, Robert G., Shivaram Rajgopal, and Jing Xie, 2022, Does ESG negative screening work? Working paper, Columbia Business School.
- Edmans, Alex, 2009, Blockholder trading, market efficiency, and managerial myopia, *Journal of Finance* 22, 2481–2513.

- Edmans, Alex, 2011, Does the stock market fully value intangibles? Employee satisfaction and equity prices, *Journal of Financial Economics* 101, 621–640.
- Edmans, Alex, 2020, *Grow the Pie* (Cambridge University Press, Cambridge).
- Edmans, Alex, 2022, The end of ESG, *Financial Management* 52, 3–17.
- Edmans, Alex, Doron Levit, and Jan Schneemeier, 2022, Socially responsible divestment, ECGI Working Paper 823/2022.
- Eckbo, B. Espen, Knut Nygaard, and Karin S. Thorburn, 2022, Valuation effects of Norway's board gender quota law revisited, *Management Science* 68, 3975–4753.
- El Ghoul, Sadok, and Aymen Karoui, 2017, Does corporate social responsibility affect mutual fund performance and flows? *Journal of Banking and Finance* 77, 53–63.
- Engle, Robert, Stefano Giglio, Bryan Kelly, Heebum Lee, and Johannes Stroebe, 2020, Hedging climate change news, *Review of Financial Studies* 33, 1184–1216.
- Fama, Eugene F., and Kenneth R. French, 2007, Disagreement, tastes and asset prices, *Journal of Financial Economics* 83, 667–689.
- Fich, Eliezer M., and Guosong Xu, 2023, Involuntarily green? Corporate donations to politicians and their votes on environmental legislation, Working paper, Drexel University.
- Field, Laura Casares, Matthew E. Souther, and Adam S. Yore, 2020, At the table, but cannot break through the glass ceiling: Board leadership positions elude diverse directors, *Journal of Financial Economics* 137, 787–814.
- Flammer, Caroline, 2021, Corporate green bonds, *Journal of Financial Economics* 142, 499–516.
- Flammer, Caroline, Thomas Giroux, and Geoffrey Heal, 2023, Biodiversity finance, NBER Working Paper 31022.
- Flammer, Caroline, Bryan Hong, and Dylan Minor, 2021, Corporate governance and the rise of integrating corporate social responsibility criteria in executive compensation: Effectiveness and implications for firm outcomes, *Strategic Management Journal* 40, 1097–1122.
- Flammer, Caroline, Michael Toffel, and Kaia Viswanathan, 2021, Shareholder activism and firms' voluntary disclosure of climate change risks, *Strategic Management Journal* 42, 1850–1879.
- Friede, Gunnar, Timo Busch, and Alexander Bassen, 2015, ESG and financial performance: Aggregated evidence from more than 2000 empirical studies, *Journal of Sustainable Finance and Investment* 5, 210–233.
- Ganchev, Nickolay, Mariassunta Giannetti, and Rachel Li, 2022a, Does money talk? Divestitures and corporate environmental and social policies, ECGI Working Paper 634/2019.
- Ganchev, Nickolay, Mariassunta Giannetti, and Rachel Li, 2022b, Sustainability or performance? Ratings and fund manager incentives, ECGI Working Paper 747/2021.
- Garel, Alexandre, Arthur Romec, Zacharias Sautner, and Alexander F. Wagner, 2023, Do investors care about biodiversity? Working Paper 905/2023.
- Garrett, Daniel, and Ivan Ivanov, 2023, Gas, guns, and governments: Financial costs of anti-ESG policies, Working paper, Wharton Business School.
- Gasparini, Matteo, and Peter Tufano, 2023, The evolving academic field of climate finance, Working paper, Harvard Business School 23–057.
- Geczy, Christopher C., Robert F. Stambaugh, and David Levin, 2021, Investing in socially responsible mutual funds, *Review of Asset Pricing Studies* 11, 309–351.
- Giannetti, Mariassunta, and Tracey Yue Wang, 2023, Public attention to gender equality and board gender diversity, *Journal of Financial and Quantitative Analysis* 58, 485–511.
- Giannetti, Mariassunta, and Mengxin Zhao, 2019, Board ancestral diversity and firm-performance volatility, *Journal of Financial and Quantitative Analysis* 54, 1117–1155.
- Gibson Brandon, Rajna, Philipp Krueger, and Peter S. Schmidt, 2021, ESG rating disagreement and stock returns, *Financial Analysts Journal* 77, 104–127.
- Giglio, Stefano, Bryan Kelly, and Johannes Stroebe, 2021, Climate finance, *Annual Review of Financial Economics*, 13, 15–36.
- Giglio, Stefano, Matteo Maggiori, Johannes Stroebe, Zhenhao Tan, Stephen Utkus, and Xiao Xu, 2023, Four facts about ESG beliefs and investor portfolios, NBER Working Paper 31114.
- Gillan, Stuart L., Andrew Koch, and Laura T. Starks, 2021, Firms and social responsibility: A review of ESG and CSR research in corporate finance, *Journal of Corporate Finance* 66, 101889.

- Gillan, Stuart L., Naciye Sekerci, and Laura T. Starks, 2022, Managerial response to investor environmental demand: The role of firm ownership, Working paper, University of North Texas.
- Gillan, Stuart L., and Laura T. Starks, 2000, Corporate governance proposals and shareholder activism: the role of institutional investors, *Journal of Financial Economics* 57, 275–305.
- Goldstein, Itay, Alexandr Kopytov, Lin Shen, and Haotian Xiang, 2022, On ESG investing: Heterogeneous preferences, information, and asset prices, NBER Working Paper 29839.
- Gormley, Todd A., Vishal K. Gupta, David A. Matsa, Sandra C. Mortal, and Lukai Yang, 2022, The big three and board gender diversity: The effectiveness of shareholder voice, NBER Working Paper 30657.
- Graham, John, 2022, Presidential address: Corporate finance and reality, *Journal of Finance* 77, 1975–2049.
- Guerard, John, 1997, Is there a cost to being socially responsible? *Journal of Forecasting* 16, 475–490.
- Hart, Oliver, and Luigi Zingales, 2017, Companies should maximize shareholder welfare not market value, *Journal of Law, Finance, and Accounting* 2, 247–275.
- Hamilton, Sally, Hoje Jo, and Meir Statman, 1993, Doing well while doing good? The investment performance of socially responsible mutual funds, *Financial Analysts Journal* 49, 62–66.
- Hartzell, Jay C., and Laura T. Starks, 2003, Institutional investors and executive compensation, *Journal of Finance* 58, 2351–2374.
- Hartzmark, Samuel M., and Abigail B. Sussman, 2019, Do investors value sustainability? A natural experiment examining ranking and fund flows, *Journal of Finance* 74, 2789–2837.
- He, Yazhou, Bige Kahraman, and Michelle B. Lowry, 2023, ES risks and shareholder voice, *Review of Financial Studies* (forthcoming).
- Heeb, Florian, Julian F. Kolbel, Falko Paetzold, and Stefan Zeisberger, 2023, Do investors care about impact? *Review of Financial Studies* 36, 1737–1787.
- Heinkel, Robert, Alan Kraus, and Josef Zechner, 2001, The effect of green investment on corporate behavior, *Journal of Financial and Quantitative Analysis* 36, 431–449.
- Hoepner, Andreas G.F., Arleta A.A. Majoch, and Xiaoyan Zhou, 2021, Does an asset owner's institutional setting influence its decision to sign the Principles for Responsible Investment? *Journal of Business Ethics* 168, 1–26.
- Hoepner, Andreas G.F., Ioannis Oikonomou, Zacharias Sautner, Laura T. Starks, and Xiao Y. Zhou, 2022, ESG shareholder engagement and downside risk, ECGI Working Paper 671/2020.
- Hong, Harrison, and Marcin Kacperczyk, 2009, The price of sin: The effects of social norms on markets, *Journal of Financial Economics* 93, 15–36.
- Hong, Harrison, G. Andrew Karolyi, and Jose A. Scheinkman, 2020, Climate finance, *The Review of Financial Studies* 33, 1011–1023.
- Hong, Harrison, and Leonard Kostovetsky, 2012, Red and blue investing: Values and finance, *Journal of Financial Economics* 103, 1–19.
- Houston, Joel F., and Hongyu Shan, 2022, Corporate ESG profiles and banking relationships, *Review of Financial Studies* 35, 3373–3417.
- Humphrey, Jacquelyn, Shimon Kogan, Jacob Sagi, and Laura T. Starks, 2022, The asymmetry in responsible investing preferences, NBER Working Paper 29288.
- Humphrey, Jacquelyn E., Darren D. Lee, and Yaokan Shen, 2012, Does it cost to be sustainable? *Journal of Corporate Finance* 18, 626–639.
- Humphrey, Jacquelyn E., and David T. Tan, 2014, Does it really hurt to be responsible? *Journal of Business Ethics* 122, 375–386.
- Hwang, Chuan Yang, Sheridan Titman, and Ying Wang, 2022, Investor tastes, corporate behavior, and stock returns: An analysis of corporate social responsibility, *Management Science* 68, 7065–7791.
- Ilhan, Emirhan, Philipp Krueger, Zacharias Sautner, and Laura T. Starks, 2023, Climate risk disclosure and institutional investors, *Review of Financial Studies* (forthcoming).
- Ilhan, Emirhan, Zacharias Sautner, and Grigory Vilkov, 2021, Carbon tail risk, *Review of Financial Studies* 34, 1540–1571.
- Kacperczyk, Marcin, and Jose Luis Peydro, 2022, Carbon emissions and the bank-lending channel, Working paper, Imperial College London.

- Karlan, Dean, Adam Osman, and Jonathan Zinman, 2021, Dangers of a double-bottom line? A poverty targeting experiment misses both targets, *Journal of Economics and Management Strategy*.
- Karolyi, G. Andrew, and John Tobin-de la Puente, 2023, Biodiversity finance: A call for research into financing nature, *Financial Management* 52, 231–251.
- Karpoff, Jonathan, 2021, On a stakeholder model of corporate governance, *Financial Management* 50, 321–43.
- Kedia, Simi, Laura T. Starks, and Xianjue Wang, 2021, Institutional investors and hedge fund activism, *Review of Corporate Finance Studies* 10, 1–43.
- Khan, Mozaffar, George Serafeim, and Aaron Yoon, 2016, Corporate sustainability: First evidence on materiality, *The Accounting Review* 91, 1697–1724.
- Kim, Daehyun, and Laura T. Starks, 2016, Gender diversity of corporate boards: Do women bring unique skills? *American Economic Review* 106, 267–271.
- Krueger, Philipp, 2015, Corporate goodness and shareholder wealth, *Journal of Financial Economics* 115, 304–329.
- Krueger, Philipp, Daniel Metzger, and Jiaxin Wu, 2022, The sustainability wage gap, ECGI Working Paper 718/2020.
- Krueger, Philipp, Zacharias Sautner, and Laura T. Starks, 2020, The importance of climate risk for institutional investors, *Review of Financial Studies* 33, 1067–1111.
- Krueger, Philipp, Zacharias Sautner, Dragon Yongjun Tang, and Rui Zhong, 2023, The effects of mandatory ESG disclosure around the world, ECGI Working Paper 754/2021.
- Liang, Hao, and Luc Renneboog, 2017, On the foundations of corporate social responsibility, *Journal of Finance* 72, 853–910.
- Lindsay, Laura Anne, Seth Pruitt, and Christoph Schiller, 2022, The cost of ESG investing, Working paper, Arizona State University.
- Lins, Karl V., Henri Servaes, and Ane Tamayo, 2017, Social capital, trust, and firm performance: The value of corporate social responsibility during the financial crisis, *Journal of Finance* 72, 1785–1824.
- Lo, Andrew W., and Ruixun Zhang, 2021, Quantifying the impact of impact investing, Working paper, MIT.
- Lowry, Michelle, Pingle Wang, and Kelsey D. Wei, 2023, Are all ESG funds created equal? Only some funds are committed, ECGI Working Paper 874/2023.
- Matos, Pedro, 2020, ESG and responsible institutional investing around the world: A critical review, CFA Institute Research Foundation.
- McCahery, Joseph A., Zacharias Sautner, and Laura T. Starks, 2016, Behind the scenes: The corporate governance preferences of institutional investors, *Journal of Finance* 71, 2905–2932.
- Naaraayanan, S. Lakshmi, Kunal Sachdeva, and Varun Sharma, 2021, The real effects of environmental activist investing, Working paper, London Business School.
- Nickerson, Raymond S., 1998, Confirmation bias: A ubiquitous phenomenon in many guises, *Review of General Psychology* 2, 175–220.
- Oehmke, Martin, and Marcus Opp, 2022, A theory of socially responsible investment, CEPR Working Paper 14351.
- Pastor, Lubos, Robert Stambaugh, and Lucian Taylor, 2021, Sustainable investing in equilibrium, *Journal of Financial Economics* 142, 550–571.
- Pastor, Lubos, Robert Stambaugh, and Lucian Taylor, 2022, Dissecting green returns, *Journal of Financial Economics* 146, 403–424.
- Pedersen, Lasse H., Shaun Fitzgibbons, and Lukasz Pomorski, 2021, Responsible investing: The ESG-efficient frontier, *Journal of Financial Economics* 142, 572–597.
- Pollman, Elizabeth, 2022, The making and meaning of ESG, ECGI Working Paper 659/2022.
- Renneboog, Luc, Jenke ter Horst, and Chendi Zhang, 2008, Socially responsible investments: Institutional aspects, performance, and investor behavior, *Journal of Banking and Finance* 32, 1723–1742.
- Renneboog, Luc, Jenke ter Horst, and Chendi Zhang, 2011, Is ethical money financially smart? Nonfinancial attributes and money flows of socially responsible investment funds, *Journal of Financial Intermediation* 20, 562–588.

- Riedl, Arno, and Paul Smeets, 2017, Why do investors hold socially responsible mutual funds? *Journal of Finance* 72, 2505–2550.
- Roy, Amlan, 2022, *Demographics Unravelling: How Demographics Affect and Influence Every Aspect of Economics, Finance and Policy* (John Wiley & Sons, Ltd, Chichester, UK).
- Sautner, Zacharias, Jing Yu, Rui Zhong, and Xiaoyan Zhou, 2022, The EU taxonomy and the syndicated loan market, Working paper, Frankfurt School of Finance & Management.
- Seltzer, Lee, Laura T. Starks, and Qifei Zhu, 2022, Climate regulatory risks and corporate bonds, Working paper, University of Texas at Austin.
- Shive, Sophie A., and Margaret M. Forster, 2020, Corporate governance and pollution externalities of public and private firms, *Review of Financial Studies* 33, 1296–1330.
- Skrancke, Martin, Elroy Dimson, Michael Hoel, Magdalena Kettis, Gro Nystuen, and Laura Starks, 2014, Fossil-fuel investments in the Norwegian Government Pension Fund Global: Addressing climate issues through exclusion and active ownership, A Report by the Expert Group appointed by the Norwegian Ministry of Finance.
- Starks, Laura T., 2009, EFA keynote speech: Corporate governance and corporate social responsibility: What do investors care about? What should investors care about? *Financial Review* 44, 461–468.
- Starks, Laura T., 2021, Environmental, social, and governance issues and the *Financial Analysts Journal* 77, 5–21.
- Starks, Laura T., Parth Venkat, and Qifei Zhu, 2022, Corporate ESG profiles and investor horizons, Working paper, University of Texas at Austin.
- Statman, Meir, 2000, Socially responsible mutual funds (corrected), *Financial Analysts Journal* 56, 30–39.
- Statman, Meir, and Denys Glushkov, 2009, The wages of social responsibility, *Financial Analysts Journal* 65, 33–46.
- Statman, Meir, and Denys Glushkov, 2016, Classifying and measuring the performance of socially responsible mutual funds, *Journal of Portfolio Management* 42, 140–151.
- Stroebel, Johannes, and Jeffrey Wurgler, 2021, What do you think about climate finance? *Journal of Financial Economics* 142, 487–498.
- Tang, Dragon Yongjun, and Yupu Zhang, 2020, Do shareholders benefit from green bonds? *Journal of Corporate Finance* 61, <http://dx.doi.org/10.1016/j.jcorpfin.2018.12.001>.
- Teoh, Siew Hong, Ivo Welch, and C. Paul Wazzan, 1999, The effect of socially activist investment policies on the financial markets: Evidence from the South African boycott, *Journal of Business* 72, 35–89.
- Tkac, Paula, 2006, One proxy at a time: Pursuing social change through shareholder proposals, *Federal Reserve Bank of Atlanta Economic Review*, 3rd quarter, 1–20.
- Whelan, Tensie, and Randi Kronthal-Sacco, 2019, Research: Actually consumers do buy sustainable products, *Harvard Business Review* June 19, 2–4.
- Whelan, Tensie, Ulrich Atz, Tracy Van Holt, and Casey Clark, 2021, ESG and financial performance: Uncovering the relationship by aggregating evidence from 1,000 plus studies published between 2015–2020, Working paper, NYU Stern Center for Sustainable Business.
- Wolf, Martin J., John W. Emerson, Daniel C. Esty, Alex de Sherbinin, and Zachary A. Wendling, 2022, *2022 Environmental Performance Index* (Yale Center for Environmental Law & Policy, New Haven, CT). Epi.yale.edu.
- Wu, Xiting, Jiaxing You, Xiaoyun Yu, and Clara Zhou, 2022, Leveling up your green mojo: The benefits of beneficent investment, Working paper, SAIF.
- Zerbib, Olivier David, 2022, A sustainable capital asset pricing model (S-CAPM): Evidence from environmental integration and sin stock exclusion, *Review of Finance* 26, 1345–1388.