HIGH SCHOOL EDITION
Journal of Student Research
Volume 13 Issue 4 (2024)

The Ramifications of Blackrock and Vanguard's ESG Investments within the 21st Century

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ABSTRACT

In the last two decades, ESG (economic, social, governance) investing underwent rapid growth that stemmed from the adoption of movements such as the promotion of sustainable development goals under the UN, shifting focus towards embedding sustainability within the social and environmental aspects of businesses. This motive was spearheaded by investment firms such as Blackrock and Vanguard, who have poured hundreds of billions to perpetuate ESG values in the market. A multitude of scholars have done extensive research into this recent shift in financial policymaking, revealing that many large businesses have elevated their stock performance by adhering to associated investor demands, while simultaneously furthering efforts to combat environmental risks. Although many have considered these positives, other researchers have outlined corruption within the corporate push to increase investment revenue through the use of 'green' agendas as well. Despite the vast diversity of perspectives on the merits of ESG investing, however, there remains a lack of comprehensive dialogue surrounding the overall outlook of the issue from all standpoints. This paper aims to analyze the economic, environmental, and ethical perspectives involved in the proliferation of ESG policies in the status quo with an underlying focus on the moral value of these ventures. It is revealed that Blackrock and Vanguard's ESG investments have ultimately degraded the effectiveness of sustainability reforms by promoting an increased focus on profits over environmentally and socially conscious developments, helping propose that additional government intervention is needed within the economy to mitigate the detrimental impacts.

Introduction

In the face of widespread social and conservationist movements in the 21st century, the status quo of corporate investment has shifted in favor of ESG (economic, social, governance) initiatives that emphasize "the belief that both society and investors benefit" through adherence to sustainable development goals (SDGs) set by the UN General Assembly (van Duuren et al., 2016). Due to the resulting changes in market dynamics, major companies have now begun to increase focus on these values and advance their own motives to improve the social and environmental impact of business operations. Kamala Raghavan, a professor at Texas Southern University, qualifies this notion and reveals that this transition is largely overseen by conglomerates such as Blackrock, Vanguard, and State Street Global, who utilize "third-party assurance" of global sustainable development goals through assessments of major corporations such as Eli Lilly, Etsy, and Johnson & Johnson with "corporate social responsibility" (CSR) metrics to determine investment priorities (Raghavan, 2022). Firms such as Blackrock aim to utilize nearly "10 trillion dollars in assets" to prioritize this movement for business improvement through billions of dollars annually, thus leading to a high level of control over the US stock market (Baer, 2019). Franklin Delano Roosevelt, the 32nd President of the United States, warned in his Inaugural speech that the prevalence of such financial motivations for the sole cause of increasing profits could play a substantial role in mitigating the effectiveness of social and economic reforms, stating that the pursuit of "material wealth" by individuals and corporations can be ultimately detrimental to the moral standing of society as a whole (Roosevelt, 1932). Therefore, by extension, the utilization of monetary stimulation by large investment firms for the advancement of ESG ideals in the market may also undermine the moral value of the goals set by the initiatives themselves, provoking concern regarding the extreme financial control Blackrock and Vanguard possess over the social, political, and economic stature of US companies. Thus, the increasingly pressing question arises: To what extent should private firms such as Blackrock and Vanguard be allowed to utilize ESG investment within the United States economy to promote sustainable development? Although financial stimulus that prioritizes these values may have some positive impacts on the value and sustainability of larger corporations, Blackrock and Vanguard should not be allowed to push for ESG goals within the US economy to a substantial extent in order to maintain the stability of the market and competitiveness of small firms, ensure the environmental integrity of businesses, and protect against the sociopolitical unethicality of using such ventures to further their reputability and revenue.

Economic Impacts of ESG Investment

First, it becomes essential that the economics of ESG in the US stock market are assessed to determine the impacts of associated policies on the firm values. Benjamin R. Auer, a professor at the Friedrich Schiller University Jena, states that although ESG implementation involves additional costs for the maintenance of sustainable business practices, it does not “harm” the companies within an investors’ stock portfolio, but rather “[increases] portfolio performance” through the employment of improved governance that allows for additional revenue to be gained on average (Auer, 2016). Through the institution of these measures, it becomes clear that the companies within the stock portfolios of Blackrock and Vanguard potentially benefit from the subsidization of sustainability through improved management structures, leading to an increase in productivity that benefits both corporations and investors. However, it becomes essential to consider the extent to which such changes impact the regulatory self-sufficiency of companies themselves. Tao Fu and Jiangjun Li of the Beijing University of Engineering and Architecture qualify Auer’s points on the benefits of subsidizing the governance values in the ESG initiative, specifying that increased emphasis on additional social reforms establishes “better cost management, employee retention, and innovation”, increasing a firm’s financial freedoms by mitigating the need for additional regulatory and legal costs related to mismanagement and negligence of these factors (Fu & Li, 2023). This helps further advocate for the proliferation of investments from Blackrock and Vanguard, as they allow for efficient supervision of economic growth without the need for excess government interference. However, Gil Cohen of the Western Galilee Academic College contends with the benefits of increased management through ESG, as a variety of S&P 500 firms often decreased in value over time when subjected to the risks regarding the successful implementation of these policies, as “20.4% of these stocks carry “high and severe” ecologically and socially-induced risks for a firm’s stock value when compared to a risk of “9.6%” for more valuable Nasdaq 100 stocks. These findings bring into question the efficacy and the applicability of ESG practices across a wide variety of US industries, as the highly tech-based Nasdaq 100 companies possess a competitive advantage over other corporations due to their decreased susceptibility to ESG-related risks in the market (Cohen, 2023). This financial discrepancy between the differing industries depicts the necessity of increased government regulation rather than a continuation of influence from large investment firms, as it becomes essential to limit the disproportionate advantages of the technology corporations by lessening these risks through government subsidization of social and governance practices or increased jurisdiction within companies themselves. Amal Aouadi and Sylvain Marsat of the University of Lille and the University of Maryland respectively corroborate Cohen’s findings, and state that ESG risks can further negatively impact small firms due to their “low levels of press freedom” and attention from investors. They state that the prevalence of ESG-related controversies has a “positive and significant” relationship with a company’s corporate social performance (CSP) score, attracting investors to large corporations that are more involved in media coverage (Aouadi & Marsat, 2018). Thus, it is not only industries outside of the technology sector that disproportionately benefit from the institution of ESG policies; larger companies in general are more prone to attract investors from Blackrock through the extensive coverage of their relations with socially or environmentally conscious policy-making. Therefore, it is essential that the influence of large investment firms is limited to bridge the widened gap in economic opportunities between smaller and larger firms, and that the government plays an increased role in the oversight of the market instead through regulatory policies.

Risks for Corporate Environmental Integrity

In addition to the economics of Blackrock and Vanguard investments through analysis of social and governance initiatives, it becomes essential to consider whether the financial incentives behind ESG policies promote business integrity in environmentally conscious decision-making. Sebastian Schmidt and his colleagues at the University of Salzburg and the Center for European Economic Research state that the "8.1%" of US metal corporations (large contributors to air pollution) that claim sustainable practices have not engaged in dishonest reporting of their impacts, as their self-reported emission statistics have aligned with the decreased sulfur dioxide emissions detected by remote sensing observations (Schmidt et al., 2022). The fact that substantial portions of such an expansive industry have truthfully implemented sustainable emission practices under ESG guidelines depicts the extent to which Blackrock and Vanguard's incentivization of these practices could positively impact companies' adherence to sustainability. This is further corroborated by Gülfen Tuna and her affiliates at Sakarya University, who state that ESG investing has remained a reliable tool for "eco-friendly investors" to respond to climate change concerns, as there is a general "causal relationship" between CO2 emission decreases and increases in ESG funding for S&P 500 companies (Tuna et al., 2023). Since the encouragement of ecological action has proven successful through the decrease in GHG emissions across multiple industries, allowing Blackrock and Vanguard to continue this prospect would enhance the US' ability to adhere to global climate goals. However, this scope does not encompass the impacts of other major US industries, such as the oil and gas sector. Mei Li and her colleagues from the Tohoku and Kyoto Universities contend with Schmidt and Tuna's notions that ESG investments from large firms actively promote environmental action. They state that although major oil and gas corporations such as Chevron and ExxonMobil have "amplified" the use of discourse that relates to their goal of "net-zero emissions by 2050," their financial plans were strongly misaligned with these ambitions, which is likely because slowing down the transition to clean energy is "profitable for the boards of these majors" (Li et al., 2022). Thus, in these sectors, it is clear that greenwashing has played a much larger role in attracting funding, leading to a substantial loss in integrity. This helps advocate for greater government regulation of corporate environmental policies through an expansion of Amendment 112 to the Clean Air Act, which establishes "emission standards" in industrial activities (EPA, 2023). Furthermore, Menno De Jong and his colleagues at the University of Twente qualify on Li et al.'s notions of the negative impacts of ESG investing, stating that resulting dishonest reporting can also alter public acceptance of eco-friendly practices. As greenwashing has negative implications on the "communicative integrity" of corporations, they note that consumers may become more "distrustful of both [fraudulent marketing] and green products in general," reducing public interest in the use of environmentally conscious business practices (De Jong et al., 2017). Therefore, in the face of growing ESG initiatives, it becomes essential to protect public interests and the adherence of businesses to conservationist claims through increased government oversight in the market with the aforementioned expansion of the Clean Air Act rather than integrating Blackrock and Vanguard's financial influence.

Ethical Implications of Financial Incentivization

In addition to the negative environmental ramifications of ESG investing, the aforementioned losses in business integrity bring into question the ethics of Blackrock and Vanguard's financial stimulus of market reform. In a study conducted by Molly Carnes and her colleagues at the University of Wisconsin-Madison, it is stated that diversity statements—major components of the social aspect of ESG—often create the perception that institutions "force pro-diversity actions on [their] members," leading to backlash from employees regarding the emphasis on "multiculturalism" instead of "colorblindness" and merit (Carnes et al., 2019). This brings into question the morality of subsidizing these motives through private investment firms, as continuing to force the implementation of social reforms under ESG investments may undermine the dissenting voices and concerns of the employee body. Ted Thomas and Ira Chaleff of the US Army and Executive Coaching & Consulting Associates in Washington D.C. corroborate the notion that strict adherence to ESG values due to incentivization is immoral, as corporate cultures that "focus on short-term gain and stifle dissent" will damage long-term success, as it is the "moral obligation" of leaders to impose ethical values in the workplace (Thomas & Chaleff, 2017). This helps further advocate for restrictions on the influence of Blackrock and Vanguard through ESG investing policies, as their use of financial investment potentially hinders the autonomy of business leaders in promoting employees' free speech surrounding concepts such as diversity. One potential solution to the issue is to mitigate concerns surrounding discrimination in corporations without neglecting employee concerns by strengthening the jurisdiction of the Civil Rights Act of 1991, helping promote equality in employee treatment rather than forced equity through ESG (Congress, 1990). Bernard S. Sharfman of George Mason University qualifies on Thomas and Chaleff's statements, asserting that Blackrock has also marginalized the needs of its own employees and beneficiaries through its "shareholder activism." He reveals that the primary purpose behind ESG ideology was "marketing to millennials" (who are currently receiving "24 trillion" in inheritance from baby boomers), resulting in "financial harm to the beneficial investors of Blackrock's index funds." These primarily consist of employees' 401k funds safeguarded under the Employee Retirement Income Security Act of 1974 (Sharfman, 2021). Due to the risks of financial harm for employees through the extreme focus on ESG practices, it becomes essential for the government to play a substantial role in moderating this extensive speculation in the market. The notion that this is a result of catering to the millennial demographic further calls the morality of ESG investing into question. Franklin D. Roosevelt qualifies on the unethicality of this venture, as the obtaining of "personal profit" should not be the cornerstone of policymaking, and asserts that banking and business should "end speculation with other people's money" (Roosevelt, 1933). Thus, it becomes essential that the government increases its role through the furthering of social reforms in place of Blackrock and Vanguard, in order to protect against the moral costs of allowing these firms to influence the market for the end goal of pursuing profits over the welfare of society itself.

Discussion

In the face of the detrimental impacts of ESG investing on the market through large firms such as Blackrock and Vanguard, it becomes essential for the government to play a much greater role in moderating speculation within the market and the integrity of impacted corporations. This can be done through the enactment of three potential resolutions: increasing government jurisdiction through the Clean Air Act, influencing workplace equality through the Civil Rights Act of 1990, and maintenance of the Employee Retirement Income Security Act. However, some limitations arise in that the solution is based on an increase in government regulation of the market, which could potentially have negative consequences for the growth of the American economy as a whole. Daniel L. Millimet and his colleagues at the Southern Methodist University qualify this point, revealing that the EPA's implementation of environmental regulations from 2004-2008 cost an "[inflation-adjusted] total of $45 billion in pollution control" and investments in "environmentally-beneficial projects" (Millimet 2014). This remains relevant in the modern day, as any additional regulations pertaining to either the environmental or social aspects of businesses in a similar manner to ESG investments will still be associated with large upfront costs. Nonetheless, the proposed solution maintains validity, as it would have proportionate impacts on both smaller and larger corporations rather than create economic disparities between companies of differing fields as asserted by Cohen et al. This implies that by incorporating these actions, no single corporation or sector will obtain a concrete advantage over others in the stock market, allowing for increased competition that would instead fuel economic growth. More importantly, the utilization of the increased regulations would adhere to the moral standpoint taken within the paper, as it aligns with Roosevelt's notion that profit generation should be deprioritized when attempting to institute economic reforms.

Acknowledgments

I would like to give a special thanks to Mr. Haisler, my AP Seminar teacher during my junior year, who gave me essential feedback on my research that would allow me to comprehensively assess this vast topic. Moreover, I would like to thank Katy ISD for providing me with numerous scholarly resources that made this paper possible.

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