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Bringing the "S" back to ESG: The roles of organizational context and institutions

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DEAR READER,

Welcome to edition 56 of the Capco Institute Journal of Financial Transformation, produced in partnership with King's Business School and dedicated to the theme of ESG – environmental, social and governance.

We all recognize that transformation towards a green economic system via sustainable finance is needed, welcome and inevitable. Our clients have a crucial role to play here. Acknowledging the scope and complexity of the evolving ESG landscape, we are perfectly positioned to prepare them for the ESG era.

With climate change accelerating and generating physical events on an unprecedented scale, governments and societies are considering measures to mitigate carbon emissions via net zero initiatives. The focus is firmly on greater sustainability and more equitable policies in response to shifting public attitudes. ESG considerations are reshaping investment risks on the one hand, and opening the way for green financing and sustainable technologies and innovations on the other.

This edition of the Journal examines all three pillars – environmental, social, and governance, highlighting efforts by regulators and practitioners to create a unified approach.

Moving forward, compliance with emerging ESG standards will be a critical differentiator for long-term business success. Data will also play a critical role in delivering the transparency and insights required to validate the ESG credentials of businesses, and investment strategies. Advances in areas such as machine learning, artificial intelligence and cloud technologies will be key to establishing a future model of sustainable finance.

This edition draws upon the knowledge and experience of world-class experts from both industry and academia, covering a host of ESG topics and innovations including the value of tracking Return on Sustainability Investment (ROSI) and the importance of moving away from purely external risks to addressing issues that can have positive commercial and societal impacts.

I hope that that the research and analysis within this edition will prove valuable for you as you shape your own ESG strategies, policies, and innovation.

Thank you to all our contributors and thank you for reading.

Lance Levy, **Capco CEO**

BRINGING THE "S" BACK TO ESG: THE ROLES OF ORGANIZATIONAL CONTEXT AND INSTITUTIONS

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ABSTRACT

Building on research on corporate social responsibility (CSR) and institutional theory, this paper explores firms' perspectives on and approaches to the "S" (the social responsibility dimension) of the ESG framework in different institutional and organizational contexts. Building on studies grounded in institutional and organizational theories we argue that the scope and effectiveness of S strategies may differ depending on the legal system and institutional characteristics in a specific country. Our discussion suggests that researchers need to develop more holistic, institutionally embedded research frameworks to analyze organizational approaches to ESG.

"During the 'rebalancing' of the S&P 500 ESG index, Tesla has been dropped as a constituent. Elon Musk, the founder, CEO and product architect at Tesla, tweeted in response: 'ESG is a scam… It has been weaponized by phony social justice warriors.' However, Margaret Dorn, the S&P Global's head of ESG indices for North America, responded that: 'The beauty of an index is that it's transparent and rules-based, and we followed the rules of the index.' The index was intended to give 'broad market exposure', and Tesla's rating fell into the bottom quartile of the automotive sector because of claims of racial discrimination and poor working conditions at one of its factories" [Mundy and Temple-West (2022)].

1. INTRODUCTION

The term ESG was coined by a group of financial institutions, invited by the then United Nations Secretary-General, Kofi Anan "to develop guidelines and recommendations on how to better integrate environment, social and corporate governance issues in asset management, securities brokerage services and associated research functions", in a joint report, "Who cares wins", published by the United Nations (U.N.) in 2004 [UNGC (2004) (i)]. The participating financial institutions endorsed the report on the basis that "better consideration of environment, social and governance factors will ultimately contribute to stronger and more resilient investment markets as well as contribute to the sustainable development of societies" [UNGC (2004) (ii)]. Organizational theorists increasingly recognize that the quest for compliance with core principles of ESG is not only an answer to various corporate scandals and the recognition that business leaders may be acting irresponsibly with regard to the environment and key stakeholders more often than previously thought [Brown and Treviño (2006)], but also a result of the changes and new demands in the global marketplace, such as increased stakeholder activism and institutional pressures [Crilly (2011)]. Although there is a substantial and rapidly growing body of research in the fields of responsible leadership and ethical decision-making [Pless et al. (2012), Stahl and Sully de Luque (2015)], this research, for the most part, has not focused on contextual factors influencing managerial decision-making in the ESG area, and surprisingly little attention has been devoted to how institutional and organizational contexts may impact on the firm's strategy in the "S" sphere, and the way it is implemented.

Thus, while previous research has advanced our understanding of the environment ("E") and governance ("G") challenges facing executives, various concepts and research streams in the "S" field have not been well integrated into a comprehensive analysis and important research gaps remain. The case of Tesla provided above is an example that illustrates how losing focus on S-related aspects could undermine the whole ESG standing, even in companies with relatively high environmental sustainability standards. This paper aims to address this important, and yet not well-researched dimension of current ESG debates.

There is a growing consensus amongst business leaders and investors that environmental, social, and governance factors are "at the core of business" as they can "have long-term consequences on a company's financial performance" [UNEP (2010)]. Since its inception in 2004, much discussion has taken place and many initiatives have been led globally by various organizations, such as the United Nations and its agencies and other intergovernmental organizations, as well as national governments, standard setting bodies, business and professional associations, rating agencies, and NGOs [Nakajima (2021)]. Nevertheless, researchers and practitioners increasingly recognize that social responsibility is more nebulous and difficult to gauge than the other two criteria [i.e., E and G). Assessing aspects of social justice and evaluating the company's social impact without adequate data and accepted methodologies appear to be challenging. More importantly, E, S, and G policies are not orthogonal – they are interrelated: decarbonization strategies may have to recognize the need for a "just transition" that takes into account the interests of those affected. More importantly, a formal recognition of stakeholder interests increases complexity in accountability [Nakajima (2012)], a core principle of "good governance".

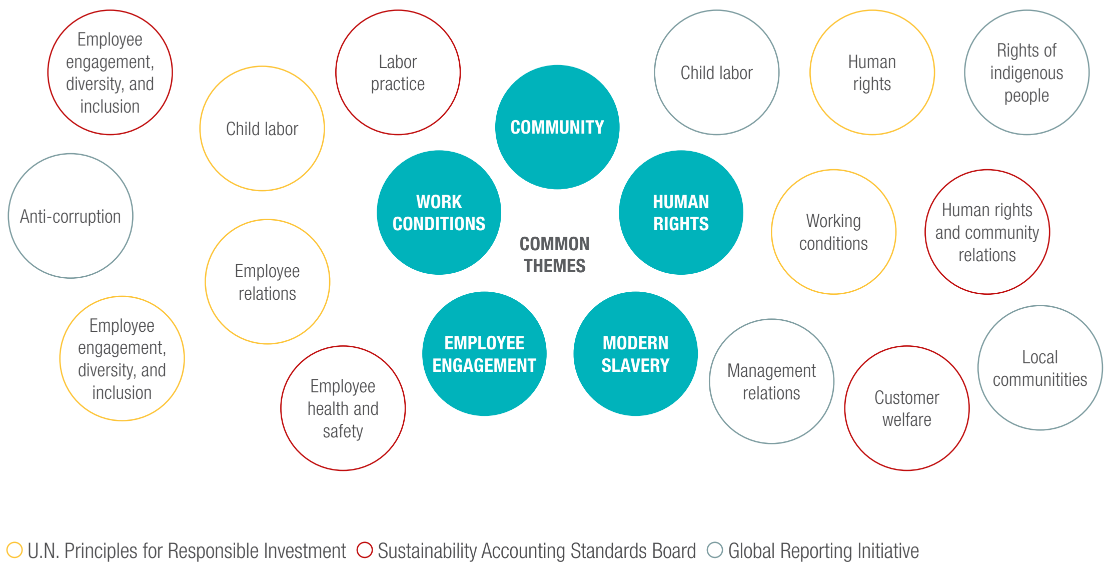
In this paper, we develop a multi-level theoretical framework that combines institutional theory and ESG perspective by focusing on a complex interplay between actions of corporate leaders – both the "do no harm" and "do good" dimensions of socially-focused behavior [Stahl and Sully de Luque (2014)] and external institutional pressures to engage in ethically responsible corporate behavior. As Delmas and Toffel (2008) suggest, organizational authority moderates perceptions of institutional pressures and thus managerial practices adopted. Although these arguments underpin earlier studies of responsible managerial behavior in economics and finance literatures, the main focus of this research was predominantly on issues of compliance with laws and regulations [Devinney et al. (2013)], including accounting rules and anti-fraud policies [Ball et al. (2003), Bushman et al. (2004)]. Lesser attention has been paid to the promoting of ESG policies that go beyond mere compliance and recognizing company responsibilities with regard to wider external stakeholder constituencies.

Finally, we will integrate both institutional and ESG perspectives on responsible leadership, in line with research on "institutions – pressure – firm" triplet [Eesley and Lenox (2006)], by showing how different constellations of institutional factors may lead to different "S" approaches on the firm level. As Ioannou and Serafeim (2012) argue: "Institutional theory long established that organizations are embedded within broader social structures, comprising different types of institutions that exert significant influence on the corporations' decision-making." Consequently, responsible managerial practices may be an outcome of the firm's responses to institutional pressures beyond a mere compliance with regulatory constraints, and key research questions within this framework are: where do the pressures come from; how do they drive legitimization processes, including changes in the firm's management approaches; and how do these changes, in turn, impact on the firm leaders' approach to ESG? By exploring these questions in the following sections, we intend to outline the existing approaches and discuss avenues for future research as well as some important managerial implications.

2. "S" IN THE CONTEXT OF LEGAL COMPLIANCE: BETWEEN "SOFT" AND "HARD" LAWS

Given their predominant focus on internal, organizational aspects of ESG, previous studies do not typically discuss potential roles of the firm's institutional environments in terms of their impact on the S strategy. The social dimension of the ESG framework refers to a firm's relationships with its stakeholders, both internal and external to the organization. Examples of criteria that a firm may be measured against include not only human capital management metrics (such as fair wages and employee engagement metrics), diversity and inclusion metrics, but also an organization's impact on the communities in which it operates and on supply chain partners, particularly those in developing economies where environmental, safety, and labor standards may be less stringent (Peterdy, 2022). As such, ensuring that human rights are protected throughout a firm's business operations is an essential part of the social domain in ESG, as illustrated in Figure 1.

Figure 1: Common "S" themes



Source: Twentyman et al. (2021)

The perceived importance of the issues that comprise the social pillar of ESG, and how companies respond to these issues, are likely to vary across different institutional and cultural contexts. Aguilera et al. (2007) suggest, however, that "because business organizations are embedded in different national systems, they will experience divergent degrees of internal and external pressures to engage in social responsibility initiatives." Consequently, contrary to the universalistic predictions of traditional research, different social, political, and historic macro-factors may lead to the institutionalization of very different views of firms' role in society on both individual and industry levels [de Graaf and Stoelhorst (2009)]. For example, research by Witt and Redding (2012) suggests that senior executives' views on the purpose of the firm and the meaning of social obligations vary across cultural and institutional contexts. These differences have significant implications for the choice of ESG strategies and approaches, as they affect leaders' perceptions of the legitimacy of stakeholder groups such as shareholders, consumers, employees, and the larger society. Several studies in the field of management and organization have taken a macro perspective and attempted to link firm-level corporate social responsibility (CSR) activities with national models of capitalism [Husted and Allen (2006)]. Cross-country differences in institutional arrangements are often used to explain differences in approaches to CSR [Aguilera et al. (2007)]. Specifically, researchers found that companies in the coordinated market economies (e.g., Germany and Japan) are more likely to take on board general stakeholder concerns compared to companies in the liberal market economies such as the U.S. and U.K. [Devinney et al. (2013)].

More recently, sociology-grounded research suggests that strategies are an outcome not only of coordinative demands imposed by market efficiency but also of rationalized norms legitimizing the adoption of appropriate governance practices [Bell et al. (2014)]. Legitimacy is the "generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate, within some socially constructed system of norms, values, beliefs, and definitions" [Suchman (1995)]. This perspective focuses more on theoretical efforts to understand how strategic decisions, including S strategies, affect the firm's legitimacy through perceptions of external assessors, or the stakeholder "audiences" [Deephouse and Suchman (2008)].

Research within institutional theory and social psychology fields differentiates between various types of legitimacy judgments that also include, in addition to instrumental (pragmatic), relational and moral dimensions [Aguilera et al. (2007), Bell et al. (2014), Ntim and Soobaroyen (2013)]. More specifically, institutional theorists predict that regulative, normative, and cognitive institutions put pressure on firms to compete for resources on the basis of economic efficiency. However, institutional pressures may also compel firms to conform to expected social behavior and demands of a wider body of stakeholders. As Ntim and Soobaroyen (2013) summarize this approach: "A major underlying assumption within an 'overarching' neo-institutional perspective is that the actors are not only competing for resources ('efficiency'), but they are also seeking ultimate legitimacy and social acceptance ('legitimation')." In other words, the ability of organization to achieve social acceptance will depend, in addition to efficiency concerns, on its ability to demonstrate moral and relational responsibility by committing to stewardship management practices, stakeholders' interests, and societal expectations [Aguilera et al. (2007)].

Research on "institutions – pressure – firm" triplet [Eesley and Lenox (2006)] suggests that these arguments may have far-reaching implications for firm-level ESG approaches and strategies. First, the firm's quest for moral and relational legitimacy may lead to changes in its approaches to corporate governance ("G") practices and processes. For example, some firms, in addition to enhancing monitoring capacity of boards, may also incorporate stakeholder engagement mechanisms into their formal governance structures by assigning responsibility for sustainability to the board and forming a separate board committee for sustainability. In this regard, in Germany co-determination system of corporate boards ensures that representatives of key stakeholders, including employees, have a direct say in governance matters [Raelin and Bondy (2013)]. A system of remuneration that involves not only financial performance benchmarks but also factors associated with longer-term sustainability may be another governance factor contributing to moral legitimacy [Filatotchev and Stahl (2015)]. Second, some companies introduce wider performance criteria and definitions of risk in their risk-movement systems that use non-financial indicators. Third, institutional and cultural factors may explain differences in ESG approaches among countries that we outlined above. The three types of legitimacy judgments are not applied universally, and their balance may differ depending on the specific institutional environment in a particular country. Devinney et al. (2013), for example, argue that in a shareholder-focused corporate environment, such as the U.S. and U.K., directors' and managers' obligations are mainly to the company and its shareholders, whereas in stakeholder-oriented societies, such as Germany and Japan, managers have to consider multiple stakeholder constituencies when making decisions. Witt and Redding (2012) in their comparative analysis show that while Japanese business leaders stressed the need for firms to contribute more broadly to society, U.S. executives were unanimous in assessing societal concerns as secondary to shareholder interests. This creates challenges in terms of compliance with "hard" and "soft" regulations associated with S factors.

More recently attention has been paid to the role of global institutions such as U.N.'s Global Compact and the institutionalization process of codes of conduct for global businesses and their value chains [Ioannou and Serafeim (2012), Kostova and Zaheer (1999)]. This exposes companies to what Bell et al. (2014) call "multiple institutional logics", and it is unclear how this exposure affects legitimation process and its implications for ESG. While corporations face a heightened level of institutional complexity resulting from heterogeneity and fragmentation of formal and informal rules, the recognition of the importance of ESG as a matter of public policy among inter-governmental organizations [Petkosky and Twose (2003)] has produced a plethora of international and regional agreements which, in turn, have encouraged governments to introduce national legislation. The resulting laws and regulations, imposing on corporations increasing and wide-ranging obligations concerning environmental, social, and governance issues, have formalized what were once corporate voluntary actions to legal requirements. In areas, identified by Cragg and McKague (2003) as issues covered by voluntary industry or business standards – namely environment, labor, corporate governance, money laundering, bribery and corruption, human rights, and corporate reporting – national legislation can now be found rendering protection, prevention, and control of these issues. Equally, it has been observed that legislation influences the substance, implementation, and communication of ESG, and that current normative ESG may constitute "pre-formal law" [Buhmann (2004)]. Furthermore, in many instances, laws may impose sanctions, regardless of culpability, when breached (e.g., environmental protection). It is also the case that many of the legislative developments have extra-territorial application, whereby one country's laws may have jurisdiction over individuals and corporations outside of the country [Filatotchev and Nakajima (2014)].

Consequently, in the context of "multiple institutional logics" the firms face heterogeneous and often ambiguous institutional pressures, and previously accepted standards of behavior, such as legal rules or self-regulation principles, become fragmented or outright ineffective. This may explain the growing heterogeneity of firm-level approaches to corporate governance and ESG despite a growing trend for harmonization through various governance codes and principles of "good practice" [Frederick (1991)].

3. "S" IN THE GLOBAL INSTITUTIONAL CONTEXT

Academic studies of the impact of informal institutions and culture indicate that companies pursue regulative legitimacy in order to demonstrate compliance with rules and regulations, but they also need to obtain socio-cultural legitimacy in order to reduce stakeholders' uncertainty and to secure their support [Bell et al. (2012)]. An organization possesses legitimacy within the socio-cultural sphere when stakeholders see the company acting in ways that are comprehensible, recognizable, and culturally supported. The meaning and effectiveness of S policies are, therefore, embedded in the very fabrics of informal and cognitive institutions that demonstrate a great degree of difference around the world. This creates significant challenges for global companies regarding their "S" approaches.

Specifically, the global environment in which multinational enterprises (MNEs) operate dramatically increases the complexity of the ethical dilemmas confronting MNEs and their leaders, as well as the diversity of stakeholders whose interests must be considered. Filatotchev and Stahl (2015) argue that, in this context, MNEs face a perennial dilemma: how to balance the need for global consistency in corporate responsibility and sustainability approaches and standards across the organization with the need to be sensitive to the demands and expectations of a diverse set of stakeholders spread across the globe. Building on the framework of "transnational CSR", these authors provide a systematic analysis of socially focused approaches in MNEs in the diverse cultural and institutional contexts. Although the authors discuss CSR approaches in general, their focus is on the S aspects, highlighting the tensions and possible trade-offs between globally integrated and locally adapted strategies. They discuss the constraints that they impose on MNE activities at both headquarters and subsidiary levels. Their argumentation is summarized in Table 1.

When MNEs emphasize global CSR consistency and integration in every country where the company operates, as opposed to giving priority to the concerns of local stakeholders, they are utilizing the globally standardized approach to CSR and stakeholder management. The perceived advantages derived from the global integration of CSR activities must clearly outweigh the perceived benefits of meeting the needs of local stakeholders. MNEs that follow the global approach to CSR tend to establish universal guidelines or codes of conduct and

Table 1: Approaches to corporate social responsibility in MNEs

	GLOBAL APPROACH	LOCAL APPROACH	TRANSNATIONAL APPROACH
EMPHASIS	Global integration/standardization	Local responsiveness/flexibility	Global integration and local responsiveness
DESCRIPTION	Headquarters' perspective and demands for consistency prevail over local concerns	Local concerns take precedence over demands for global consistency	Attempts to reconcile the tensions between global and local concerns
BENEFITS	Ensures consistency in managerial decision making and CSR activities; establishes clear rules of conduct; facilitates transfer of CSR best practices; helps to prevent and manage financial and reputational risks; and helps build trust and goodwill among global stakeholders	Ensures responsiveness to local conditions; greater flexibility in terms of CSR strategies and activities; and helps build trust and goodwill among local stakeholders	Provides a global "template" for coordinating the firm's CSR activities to ensure consistency, but allows executives of local subsidiaries to adapt that template according to their needs and circumstances; and may lead to high CSR performance at both headquarter and subsidiary levels
DANGERS	May lead to cultural arrogance and "ethical imperialism"; neglect of local stakeholder interests; and entice managers to blindly apply the firm's global policies without considering local circumstances	May promote a naïve form of ethical relativism ("When in Rome, do exactly as the Romans do"); make it difficult to determine what is morally right; lead to neglect of global stakeholder interests; make it difficult to create or apply universal norms and standards; and may promote tolerance for rogue states and corrupt regimes	Often difficult to strike an appropriate balance between global consistency and local adaptation; and high coordination costs and difficult to implement

Source: Filatotchev and Stahl (2015)

apply them to every cultural context in which they operate. Implicit in this approach is the assumption that universal principles of responsible conduct exist that transcend values and norms of particular societies. Business ethics scholars Thomas Donaldson and Thomas W Dunfee (1995) refer to such universal principles as "hypernorms" and assert that they are based on values "acceptable to all cultures and all organizations." Examples of such universal norms and values appear in the U.N. Global Compact and the U.N. Sustainable Development Goals.

Filatotchev and Stahl (2015) outline the evident benefits of a global approach to CSR. It establishes clear rules of behavior, increases trust in the firm's leadership and control mechanisms, helps the company prevent and manage risk, fosters a culture of responsibility within the global organization, and ensures global consistency in managerial decision making and behavior. However, such global consistency comes at a price. A global CSR approach can lead to cultural arrogance and ethical imperialism, which induces executives to act everywhere in the world in the same way as "things are done at headquarters". A global CSR approach also makes it more likely that managers use their companies' global policies to legitimize actions that are detrimental to the interests of local stakeholders or turn a blind eye to human rights abuses in the countries where they operate.

The locally-oriented approach to CSR is in some ways the mirror opposite of the global approach. It highlights the need for responsiveness to local conditions and sensitivity to the needs and demands of stakeholders in the countries where the company operates. Executives of companies that have implemented a local CSR approach thus aim to behave in a socially desirable manner, as defined by the local majority for each country where they conduct business. The locally adapted CSR approach, therefore, requires that subsidiary managers work as cooperatively as possible with local stakeholders.

The main benefit of this approach compared with the global CSR approach is its greater responsiveness to the concerns of stakeholders in the countries in which a multinational company operates. The greater flexibility and responsiveness with respect to CSR derived from a local approach is not without problems though. In practical terms, this approach makes it very difficult to create or apply any universally accepted norms or standards, or even to determine what is ethically right or acceptable. Moreover, in combination with weak institutions, inadequate regulations, and ineffective law enforcement in the countries where MNEs operate, a local CSR approach may promote unethical practices and lead to disastrous decisions at the local level.

Filatotchev and Stahl (2015) advocate for a transnational approach that adopts a hybrid strategy, based on the assumption that global and local approaches to CSR are not mutually exclusive. In many cases, economic needs, political pressures, and stakeholder expectations demand that companies respond to both global issues and local concerns simultaneously, thereby acknowledging that diverse contexts and multiple stakeholder interests require complex CSR strategies. In essence, a transnational CSR approach demands that companies develop a global template for their CSR activities to guide managerial decision making and ensure consistency across the organization, but at the same time allows executives of local subsidiaries to adapt that template according to their specific needs and circumstances. Global policies and codes of conduct may thus be enacted in different ways, depending on local cultural norms and stakeholder demands. Although the transnational approach is not without problems – in particular, it is often difficult to strike an appropriate balance between global consistency and local adaptation – this approach appears best able to guide managerial decision making, as well as to help executives address the CSR challenges in the global arena.

4. CORPORATE ATTEMPTS TO PUT THE "S" BACK INTO ESG: AN EXERCISE IN WINDOW-DRESSING OR CORPORATE SOCIAL RESPONSIBILITY IN ACTION?

As evidenced by the growing number of companies that have adopted "profit-with-purpose" business models [Levillain et al. (2019)], the emergence of dedicated ESG departments in many companies and the proliferation of voluntary codes like the U.N. Global Compact, many companies have taken some form of action to align their activities with the needs of stakeholders inside and outside the organization, with the goal of addressing some of the societal challenges we face and creating "shared value" [Porter and Kramer (2011)] through their business activities. An example is Unilever and its "Sustainable Living Plan" aiming to fully decouple growth from its overall environmental footprint and to increase its positive social impact. This was followed by an even more ambitious plan, the Unilever Compass, which lays out a number of multi-year priorities that cover the full spectrum of Unilever's business and wider ecosystem, including climate change, gender equality, human rights, and fair value. Unilever's CEO, Alan Jope, is convinced that "[t]he pressures on the planet are getting worse, and social inequality has reached a critical point. … As the world is changing increasingly quickly, our employees, our customers, our suppliers, our partners expect more from us. We know that we can continue to lead the charge, but we need to be better, bolder, and faster" [Unilever (2021)].

Studies show that firms may benefit economically from incorporating social responsibility and sustainability principles into their strategies and core business processes [Eccles et al. (2014)]. At the same time, however, many firms continue to engage in tendencies of "greenwashing" – demonstrating symbolic social or environmental responsibility while leaving the core business untouched [Crilly et al. (2012), Wright and Nyberg (2017)]. CSR still fundamentally serves as a compliance and risk-management function in most companies and is largely decoupled from the strategy, playing a predominantly ceremonial role in response to legitimacy pressures, as opposed to a substantive (i.e., tangible, measurable, and impactful) role. In the former case, firms are merely seeking to appear to be committed to the "S" in ESG to placate various stakeholder groups or avoid legal problems (e.g., discrimination lawsuits) and other negative consequences; in the latter, firms make genuine attempts to incorporate sustainability and social responsibility into their business models, cultures, and operating processes.

A glaring example of "greenwashing" is Volkswagen. Volkswagen was a member of the U.N. Global Compact until shortly after the scandal (they were delisted in the wake of the scandal) and their core values, as stated on the corporate website, included social responsibility and sustainability – all the while lobbying governments to cut back environmental regulations and cheating on emissions testing results.

Volkswagen is an extreme example, but this sort of misalignment between a company's policies and stated values and the lived values – what is actually practiced in the organization – is common. A recent study of 100 of the largest global companies that have committed to advancing the U.N. Sustainable Development Goals (SDGs) found that "the commitment of almost every company appears to be merely cosmetic; existing CSR initiatives were simply relabeled with the relevant goals. … Hardly any companies are doing anything new or different in their core business activities to advance the goals." The authors also observed that "in many cases, companies' core business activities even seem to contradict their commitments," citing ExxonMobil and Philip Morris as examples [Kramer et al. (2019)]. Thus, the fundamental challenge for companies is to fully integrate social responsibility into their business models and core operating processes and to build cultures that support the necessary transformation that will allow them to put the "S" back into ESG.

5. DISCUSSION

Our analysis outlines an emerging agenda for companies and investor community. Clearly, an effective S strategy requires recognition of complex impacts of the company's industry and institutional environments. Specifically, the integration of the "S" factor goes beyond legal and regulatory compliance, which, as observed earlier, is becoming increasingly complex due to an expanding number of international treaties and resulting national laws and regulations. Equally, what cannot be ignored is a growing body of best practice, codes of conduct, international standards, and such like – what is generically referred to as soft law. While it is not backed by the force of law, disregarding soft law may lead to negative consequences for corporations, such as shareholder actions; the loss of investors, customers, and staff; the collapse of share prices; and reputational damage. Furthermore, an increasing trend in some countries, such as the U.K., to introduce criminal liability in regard to companies failing to prevent certain actions taken by their employees or anyone acting on their behalf, such as bribery, tax evasion and fraud, has necessitated corporate leaders to consider more nebulous and harder to gauge aspects of management, such as corporate culture, and places under the microscope ethical behavior of companies and, therefore, their leaders.

As we have alluded to earlier in this article, there are various interdependencies, tensions, and trade-offs both among the social, environmental, and governance dimensions of the ESG framework and their relationship with economic outcomes such as shareholder returns, and it is a major management challenge to reconcile these tensions. When leaders are confronted with tensions such as shareholder value maximization versus serving the interests of other stakeholders, they tend to have one of two choices. They can either frame the seeming conflict in "either/or" terms, whereby the needs of one set of stakeholders take precedence over another; or they can view these tensions in "both/and" terms, looking for a resolution that meets the needs of seemingly disparate stakeholder groups [Waldman et al. (2020)].

There is a growing body of research that suggests that a "both/and" approach that follows an integrative logic and considers the needs and interests of a broad group of stakeholders, including the shareholders, is the most beneficial for the company. This approach seems to serve the needs of shareholders better than a narrow focus on profits and shareholder value maximization. For example, a study involving more than 500 CEOs and their organizations spread across 17 countries on five continents found that executive decision making that gives equal priorities to satisfying the needs of multiple stakeholder groups (e.g., shareholders/owners, employees, customers, and the greater society) resulted in stronger firm financial performance, as compared to decision making that focuses more narrowly on financial goals (e.g., costs, market share, and profits) [Sully de Luque et al. (2008)]. This more integrative orientation that attempts to reconcile economic imperatives with social and/or environmental considerations is exemplified by business leaders who have attempted to run their corporations with multiple objectives and potentially conflicting bottom lines in sustainable ways.

A prime example is former Unilever CEO Paul Polman, who initiated the "Sustainable Living Plan" – Unilever's blueprint for addressing the ecological and social challenges of our time. Polman is convinced that "if we focus our company on improving the lives of the world's citizens and come up with genuine sustainable solutions, we are more in synch with consumers and society and ultimately this will result in good shareholder returns." Polman insists that "we shouldn't talk about purpose over profits. We truly believe that by positioning our brands on doing real good, by running our supply chain in a sustainable way, by being a responsible employer and creating great opportunities for people, …then our shareholders will be well rewarded" [Massar (2020)]. The results bear him out: Unilever created twice the market growth and 300 percent shareholder return in the 10 years after implementing its Sustainable Living Plan.

As the Unilever example illustrates, purpose-driven companies and leaders recognize that making profits and creating shareholder value are prerequisites for pursuing a broader social mission. This implies that engagement in corporate responsibility and sustainability should not become an excuse for underperformance. Perhaps the biggest governance challenge in many multinationals today is making sure that purpose and profits are aligned [Pucik et al. (2022)]. In 2021, Artisan Partners, a long-term investor in Danone, issued a statement indicating that "on almost every measure, Danone's performance has lagged. Revenue has underperformed relevant category growth rates, margins are below its peer group, and return on equity and capital have stagnated or declined" [Segal (2021)]. While Artisan acknowledged that the chairman and CEO Emmanuel Faber, the force behind Danone's ESG strategy, had transformed Danone into a more environmentally sustainable and socially responsible company (the E and S in ESG), it argued that he had neglected the G of corporate governance. After several weeks of public debate, Faber was ousted from Danone. Thus, bringing the "S" back into ESG (or the "E", for that matter) cannot be achieved at the expense of the "G".

The debate surrounding the categorization of ESG and the quest for acceptable metrics continue, and the broad nature of the "S" factor poses a challenge to the business and investment sectors alike. While an agreement on at least some of the core elements that constitute the "S" might be helpful, it is arguable that businesses should strive "to do the right thing" for all stakeholders, instead of defining ESG categorization and metrics [Twentyman et al. (2021)]. However, doing "the right thing" ultimately requires human judgment. As Charkham and Simpson (1999) observe, "There is a relentless pressure to replace judgement with formulae... This rests in part on the fallacy that numbers are more precise and accurate than words. As anyone who has compiled a set of accounts knows, almost every number is a judgement."

To conclude, our discussion indicates that the changes and new demands in the global marketplace, such as increased stakeholder activism and institutional pressures, require timely and effective strategic responses from modern business and their leaders. While previous research has advanced our understanding of the environment ("E") and governance ("G") challenges facing executives, various concepts and research streams in the "S" field have not been well integrated into a comprehensive analysis. Our paper makes a call to researchers and practitioners to develop multi-level theoretical frameworks that combine the institutional theory and ESG perspective by focusing on a complex interplay between actions of corporate leaders and external institutional pressures to engage in ethically responsible corporate behavior.

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