Green | Finance

'Social Washing' Is Becoming Growing Headache for ESG Investors

Photographer: Brent Stirton/Getty Images

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ESG investors face a new threat in the age of coronavirus: "social washing."

Much like the greenwashing that exaggerates or misrepresents the environmental credentials of a project or a company, social washing can occur when the impact of an investment on labor rights or human rights are falsely overstated, said Arthur Krebbers, head of sustainable finance for corporates at Royal Bank of Scotland Group Plc's NatWest Markets unit. And it's a growing risk as investors focus more attention on social issues.

Blaze Triggers Alarm Over Rapid Growth of Big Batteries

The Coronavirus outbreak is awakening fund managers who consider environmental, social and governance issues when investing to blind spots in their analysis of companies. While fighting climate change has been the top priority for many ESG funds, the spreading pandemic is prompting investors to put a greater emphasis on the "S" of ESG and consider how companies treat employees during the pandemic.

Krebbers's comments followed the Principles for Responsible Investment, the biggest network of responsible investment firms, which said last month that ESG investors must up their game to hold companies accountable for social issues. The PRI emphasized how the lack of paid sick leave or benefits has left many workers in precarious positions during coronavirus lockdowns.

"The big challenge with social is the data," Krebbers said. "The reporting tends to be more localized and it's harder to define, especially when you compare to environmental issues where the carbon footprint provides for a well-understood, comparable metric. A lot more thought and analysis is required if we are to avoid 'social washing' situations."

Misleading Guidance

The risk of being misled by false information will only increase as more attention is given to social issues.

A number of prominent ESG-focused money managers say they're now increasing their emphasis on the "S."

As investors zero in on social issues, they'll likely focus in the short-term on what Covid-19 relief companies are providing for communities, consumers and other stakeholders, said Kara Mangone, chief operating officer of Goldman Sachs Group Inc.'s sustainable finance group. Over the longer term, investors will ask questions about companies' process and oversight, as well as how the board is engaged on these topics, she said.

"There should be a bit more rigor around the analysis of social now," said Mangone. ''If you think about the heavy emphasis on risk and disclosure around climate, we're nowhere near that on the social side."

The rapid growth of ESG funds -- more than $30 trillion is now managed in accordance with ESG principles -- has created an opportunity for chancers and swindlers.

'Bluewashing' to 'Pinkwashing'

While greenwashing may be the best known con, ESG investors face a litany of other risks. There's also "bluewashing" (using a United Nations affiliation to confer underdeserved sustainability credentials), "pinkwashing" (for false LGBTQ claims) and "rainbow washing" (to reflect inappropriate use of the UN's sustainable development goals logo), according to Steve Waygood, chief responsible investment officer at Aviva Investors in London.