ESG Is Not Impact

By Jasjit Singh , INSEAD

ESG efforts are essential for reducing harm, but it is not the same as striving for a net positive impact.

More companies than ever are now including environmental, social and governance (ESG) considerations in their strategies, and financial institutions are demonstrating significant appetite in funding them through "ESG investing". Given this trend, it is natural to wonder why we still need a separate conversation about "impact". This doubt arises because the distinction between ESG and impact remains unclear, especially as both terms are used interchangeably with "sustainability". ESG and impact are both important, but they are two different things.

At its core, ESG is about identifying societal factors that materially affect business success and managing these as business opportunities and risks. In other words, ESG's primary focus revolves around aligning societal engagement with the commercial success of the business. The hope is still that ESG efforts do also lead to more desirable social and environmental outcomes – provided they do not result in greenwashing or crowd out broader societal activities like advocacy and policy reform. But we must have realistic expectations about what ESG can and cannot achieve, as ESG efforts are ultimately driven by the "business case" and not by impact maximisation as an end goal.

Consider a fast fashion company with an ESG strategy to reduce the environmental footprint of each unit they sell. If its business model entails aggressively selling large quantities of a cheap product, its aggregate impact is still likely negative. In fact, a narrowly designed ESG strategy can even **make matters worse**, for example, if consumers start buying more of the product because they now perceive it as “green”. Even in scenarios where ESG does reduce the aggregate harm a specific company causes, mitigating this harm is not the same as moving towards real solutions to the grand challenges humanity faces.

As I discuss with **Katell Le Goulven**, Executive Director of the Hoffmann Global Institute for Business and Society, in an accompanying podcast for INSEAD’s “Mission to Change” series, pursuing impact entails getting rigorous about your approach and asking difficult questions about whether and how you really make a **net positive contribution** to the world.

A matter of intentionality

Leaders of impact-driven companies build their entire business around the guiding principle of impact, a process commonly referred to as either **social entrepreneurship or impact entrepreneurship**. The distinction between ESG and impact involves understanding the intentionality – the fundamental purpose behind an organisation’s activities.

In the case of ESG, societal engagement is a means to an end, the end being long-term business success. For impact, contributing to society is an end in itself, one that serves as a North Star for all strategic decisions. The term “sustainable business” is commonly used to refer to companies that pursue ESG. Impact goes further.

Impossible Foods is an example of a company fundamentally guided by impact. Its founder Pat Brown left a safe academic career to pursue a risky climate venture, driven by an observation that transforming the food sector offers a **promising opportunity to fight climate change**. His idea was to find a way of scaling up plant-based substitutes for meat and dairy products to reduce the devastating **impact of excessive animal farming**. Rather than building a company selling vegetarian products to vegetarians, he decided that maximising impact for him entailed getting meat lovers to consume less meat by offering them plant-based options they found genuinely appealing.

This doesn't mean that the commercial aspect does not matter for impact: A financially robust and scalable business model can in fact be critical for achieving long-term impact. Depending on the context and goals regarding the **depth vs. breadth of impact**, some entrepreneurs strive to build "impact businesses" that are financially competitive, while others create "social enterprises" that accept financial compromises in their quest for unique impact. The result is a range of businesses that contribute in different ways, something I have previously referred to as the "**intentionality spectrum**".

Starting with critical societal needs

While ESG emphasises integrating more responsible practices within existing business models, impact entrepreneurship starts with a clear intention to achieve precisely defined impact from the outset. The approach centres around problem solving, though still with a view to craft financially viable business models when possible. The distinguishing characteristic of impact entrepreneurship is a commitment to the impact goals as an end in itself.

To further clarify the difference between ESG and impact, consider the challenge of reducing **emissions in the aviation industry**, a growing sector that is hard to decarbonise as existing solutions are not very effective or scalable. The industry's climate impact is also contentious as it results largely from a small fraction of humanity that flies frequently, with the richest **10 percent accounting for over half of the emissions**. Companies pursuing ESG targets often use voluntary carbon offsets to claim carbon neutrality, despite **scientists' concerns** about the effectiveness of **cheap carbon credits**.

But impact-driven ventures are trying to find real solutions. For example, **ZeroAvia** is using hydrogen-electric technology to develop zero-emissions engines that could ultimately be deployed in both new and existing aircraft. ZeroAvia CFO and INSEAD alumna, Katya Constant, explained: "We started off with a problem statement, we didn't start off thinking that hydrogen has to be the way forward. We identified the issue, and then reviewed all the different ways that one can decarbonise the sector. We concluded that hydrogen electric is the best way forward on a climate impact basis, but also in terms of the fundamental scalability of the technology and therefore on a net impact basis."

Complementarities across the spectrum

The fact that impact entrepreneurs are not content with just pursuing ESG doesn't mean that ESG is not important. Given how the economy currently works, it is unlikely that large companies can make impact a top priority. It is generally a good thing when they still try to improve their societal performance, even if it's in the service of business interests. Nevertheless, ESG alone cannot achieve the transformative change needed given the **scale and urgency** of the social and environmental issues.

For business to fully contribute towards solving global challenges, concerted efforts are needed across the spectrum – from sustainable businesses to impact businesses and social enterprises. Although ESG is important for steering society away from impending crises, we critically need entrepreneurs, businesses and investors to go further in embracing impact. These two approaches are not mutually exclusive. The success of impact entrepreneurs often hinges on their ability to tap into the resources of large firms driven by ESG. Impact-driven employees inside large companies (so-called "intrapreneurs") can themselves play a pivotal role in driving **positive change from within**.

In all of this, policy has a critical role in setting the rules of the game. For example, the primary reason climate change is a central piece in any ESG agenda today is not the moral case for it, but the fact that companies expect regulators to make them pay more for their greenhouse gas emissions.

It is tempting to conclude that the world's biggest problems could be solved just through stringent government policies. For example, tackling global warming would involve setting a high worldwide carbon tax and using the proceeds to fund climate justice initiatives In practice, **policy solutions are rarely perfect**. Therefore, proactive business action, encompassing both ESG and impact, remains critical for societal progress.

Find article at

https://knowledge.insead.edu/responsibility/esg-not-impact

About the author(s)

Jasjit Singh is a Professor of Strategy and the Paul Dubrule Chaired Professor of Sustainable Development at INSEAD.

About the series

Crossroads: Business & Society

The **Hoffmann Global Institute for Business and Society** at INSEAD explores the intersection of business and society. The challenges of our times are unprecedented, and the decisions made by leaders today determine the future. HGIBS aims to equip these leaders to make decisions in ways that deliver positive outcomes for business, communities, people and our planet in line with globally agreed sustainability goals.

The UN Sustainable Development Goals offer a cohesive and centralised framework for discussing a new development model that is good for all people and the planet. INSEAD is aligning more closely with the SDGs as more businesses use the 17 global goals to enhance their contributions to society.

This series provides much-needed clarity regarding what the SDGs mean for strategies, operations and business models.