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THE S IN ESG- WHY COMPANIES' STANCE ON SOCIAL ISSUES MATTER

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& KARNICA BHATIA

Amidst escalating dialogues on climate change, sustainability, human rights, and social welfare, there is an increasing demand for organizations to embody the principles cherished by individuals.¹ In this evolving landscape, the paper delves into the longstanding concept of ESG, capturing significant attention in today's corporate realm. While scholars may dispute the claim that ESG concerns have seldom commanded more focus than at present, it is noteworthy that the 'social' dimension of risk is the least acknowledged and quantified facet within the ESG framework.²

At its essence, social in ESG pertains to human rights and equity within an organizational framework, encompassing interactions, policies, and actions that impact individuals, groups, and society. Within the business context, it scrutinizes all human interactions through the lenses of ethics, justice, and concern for well-being, addressing aspects such as inequality, working conditions, human rights, product safety, community relations, and supply chain transparency.³ Successful adoption of the social pillar in ESG acknowledges that businesses operate within an inherently unequal societal context. In the realm of ESG's "S," the paramount consideration is "rights," with employees, community groups, and national populations holding rights codified by law, cultural precedents, or ordinances.⁴ Companies often find themselves at the forefront of efforts to safeguard these rights, irrespective of their inclination for such a role. Companies increasingly find themselves entangled with complex social issues and it becomes inevitable for them to adapt accordingly.

¹ ECOSOC 'Achieving sustainable development and promoting development cooperation' Dialogue (19 December 2008).

² Leonardo Becchetti, and others. 'Going Deeper into the S of ESG: A Relational Approach to the Definition of Social Responsibility'(2022) 14(15) Sustainability, <<https://doi.org/10.3390/su14159668>> Accessed 12 February, 2024.

³'What Is the "S" in ESG?' (*S&P Global*, 24 Feb, 2020) <<https://www.spglobal.com/en/research-insights/articles/what-is-the-s-in-esg>> Accessed 12 February, 2024.

⁴ *ibid.*

In contributing to the relatively sparse literature on the social facet of ESG, the authors advocate for the incorporation of the company's stance on social issues in the larger framework of the S in ESG. They assert that addressing these aspects can impact the decisions of diverse stakeholders, fostering sustainable and resilient growth by cultivating a positive public image through active social engagement. To substantiate their argument, the authors employ case studies featuring diverse topics, including veganism, the controversy regarding renowned clothing brand Shein, and ongoing geopolitical conflicts such as the Ukraine-Russia war and the Gaza-Palestine situation. Additionally, the paper elucidates key concepts integral to this discussion, enhancing the clarity and effectiveness of the authors' assertions.

Companies exert influence, whether direct or indirect, on the well-being of employees, workers in the value chain, customers, and local communities.⁵ Proactive impact management is crucial in navigating these intricate relationships. This paper initiates an exploration into the nuanced ways social aspects influence a company's performance, considering both short-term and long-term perspectives. Key stakeholders, notably investors and consumers, are integral to the foundational structure of a company, thus, underscoring the imperative to delve deeper into their roles and dynamics within the organizational framework.

Social factors affecting choices

Beginning with investors, who play an active role in actively engaging with companies on social issues, employing diverse strategies to gather information and advocate for transformative changes.⁶ One prevalent and comprehensive approach is "ESG integration," where fund managers assess environmental, social, and governance risks alongside traditional financial considerations.⁷ This not only enhances financial returns but also contributes to more effective risk management. Some investors go beyond this by adopting a proactive stance, explicitly excluding stocks that do not align with their values, particularly those associated with weapons manufacturing, pornography, or tobacco.⁸ Taking it a step further, impact investors

⁵ Lise Kingo. 'The UN Global Compact: Finding Solutions to Global Challenges' (2019) United Nations, <<https://www.un.org/en/un-chronicle/un-global-compact-finding-solutions-global-challenges>> Accessed 12 Feb, 2024.

⁶ OECD (2011), The Role of Institutional Investors in Promoting Good Corporate Governance, Corporate Governance, OECD Publishing. <doi: 10.1787/9789264128750-en> Accessed 13 February, 2024.

⁷ Horton, Cole. 'Explainer: What Is the "S" in ESG Investing?' (*Reuters*, 19 July 2022) <<https://www.reuters.com/business/sustainable-business/what-is-s-esg-investing-2022-07-19/>> Accessed 13 February, 2024.

⁸ *ibid.*

seek investments that generate measurable social benefits.⁹ This involves tracking metrics such as job creation at or above a living wage or evaluating education investments based on hours of training per employee. In instances where engagement with companies on social issues proves ineffective, shareholders have the authority to propose and vote on resolutions.¹⁰ These resolutions can prompt management to conduct human rights risk assessments or disclose internal pay disparities, emphasizing the accountability of companies to their stakeholders. To illustrate and elaborate on these points, the authors utilize a case study approach, examining the examples of veganism and the fast-fashion brand Shein. These case studies serve to provide concrete examples and insights into how investors' engagement with companies on social issues can manifest in real-world scenarios, offering valuable lessons and perspectives for further exploration.

Vegan businesses inherently commit themselves to an elevated ethical standard, showcasing a dedication to innovation and a continual assessment of their supply chains.¹¹ Their relentless pursuit involves offering products and services aligned with a more sustainable and just world, placing them at the forefront of positive change. This commitment extends beyond mere economic participation, fostering job creation, introducing groundbreaking products, enhancing services, and presenting an innovative economic model. Beyond the ethical considerations, it's noteworthy that vegan businesses can be financially lucrative.¹² The plant-based meat industry, indicative of this shift, witnessed an estimated value of \$4.3 billion in 2020, with projections soaring to \$8.3 billion by 2025.¹³ Notably, Beyond Meat, a plant-based meat company that went public in 2019, reported a substantial revenue increase, reaching \$94.4 million at the end of Q3 in 2020.¹⁴ This burgeoning success underscores the attractiveness of the vegan industry as an ethical and lucrative field for investors seeking sustainable choices. Conversely, the fast-fashion brand Shein grapples with challenges in maintaining its predominant position in the clothing market. In a bid to recover, Shein actively seeks new investors, even contemplating a debut on the US stock markets, despite potential obstacles

⁹ *ibid.*

¹⁰ Victor Barros, and others 'Shareholder Activism and Firms' Performance.' (2023) 64 *Research in International Business and Finance*, <<https://doi.org/10.1016/j.ribaf.2022.101860>>, Accessed 14 February, 2024.

¹¹ Lee Park and others, 'Vegan Luxury for Non-Vegan Consumers: Impacts on Brand Trust and Attitude towards the Firm' (2024) 77 *Journal of Retailing and Consumer Services*, <<https://doi.org/10.1016/j.jretconser.2023.103669>>, Accessed 14 February, 2024.

¹² Sandra Nomoto 'Why Becoming a Vegan Business Can Multiply the Positive Impact' (*Medium*, 25 January 2021), <<https://bthechange.com/why-becoming-a-vegan-business-can-multiply-the-positive-impact-856c17abc777>>, Accessed 14 February, 2024.

¹³ *ibid.*

¹⁴ *ibid.*

posed by the United States Congress.¹⁵ The company faces skepticism from legislators regarding its alleged use of forced labor in product manufacturing—a contentious issue that could hinder its listing in the U.S. if proven true, making it difficult for the company to get investments. This scenario accentuates the critical role that social aspects play in investment decisions, particularly those rooted in ethical and sustainable considerations. The divergent paths of vegan businesses and fast fashion giants serve as poignant examples of the far-reaching impact of a company's social stance on its financial standing and investor appeal.

Proceeding with consumers who are in the modern technological landscape, moving beyond mere consumerism, making deliberate and ethical choices that contribute to the broader community.¹⁶ The significance of ethical supply chains has risen, capturing the attention of both capital markets and younger consumers who are particularly interested in understanding how a company's profit generation impacts racialized, marginalized, or vulnerable populations.¹⁷ Traditional metrics of value, such as stock price and quarterly profitability, have evolved to encompass the very nature of profit itself. By prioritizing core values like honesty, transparency, and consumer well-being, businesses have the opportunity to foster enduring customer relationships founded on mutual respect and ethical business practices. This commitment positions them as responsible market players dedicated to maintaining the highest standards of customer service and satisfaction. Drawing parallels with the aforementioned case studies, similar principles can be applied to consumers, reinforcing the notion that ethical considerations and a commitment to responsible business practices resonate with them and contribute to a company's success in the contemporary market.

Amidst the rising interest in a plant-based or vegan lifestyle, there exists a significant opportunity for vegan companies to not only capitalize on this trend but also contribute to positive global change. Recent market research highlights that Generation Z and younger millennials exhibit a 22% higher likelihood than the general population to embrace plant-based

¹⁵ Sanvi Bangalore, 'Shein's Mounting Ethical Concerns May Be Pushing Some Gen Z Shoppers to Look Elsewhere' *CBS News* (11 August, 2023) <<https://www.cbsnews.com/news/shein-controversy-why-is-it-so-popular/>> accessed 13 February, 2024.

¹⁶ Celecia Johnson, 'The Rise of Ethical Consumption: A New Era of Consumerism' (*ET Edge Insights*, 31 August 2023) <<https://etinsights.et-edge.com/the-rise-of-ethical-consumption-a-new-era-of-consumerism/>> accessed 13 February, 2024.

¹⁷ Mario Nokmi, 'The Importance of Supply Chain Ethics and Compliance and Top 6 Best Practice Tips for Every Company,' (*Polonious*, 19 January 2022) <https://www.polonious-systems.com/supply_chain_ethics_and_compliance/> accessed 13 February, 2024.

alternatives in their diet.¹⁸ Moreover, 35% of surveyed Gen Z members expressed a desire to adopt a meat-free lifestyle by 2021.¹⁹ Catering to this demographic by eliminating animal products could prove advantageous for a company's long-term success. This shift towards ethical consumption extends beyond the food industry, as established fashion brands like Versace and Gucci increasingly distance themselves from animal fur, recognizing the ethical concerns inherent in an animal-based supply chain.²⁰ Similar transformations are evident in the beauty, automotive, interior design, investment, and travel sectors. In the realm of beauty products, a study by Thuy Le emphasizes that committed vegan consumers are inclined to choose vegan cosmetics.²¹ The author argues that the strength of this inclination is tied to subjective beliefs, personal experiences, and social encouragement. A positive attitude towards veganism not only draws individuals closer to adopting this lifestyle but also reflects their concerns for environmental issues, animal rights, health considerations, and aesthetics. This makes companies manufacturing vegan products an attractive choice for the younger generations to showcase their solidarity with a particular value. Contrasting this ethical trend is the case of fast fashion giant Shein, whose recent financial downturn is attributed to a combination of poor results, the global economic slowdown, and heightened interest among young consumers in sustainability.²² The crisis deepens as customers increasingly demand transparency in production methods and fair treatment of Shein workers. As ethical violations mount, particularly concerning allegations of unsustainable manufacturing practices, Gen Z consumers, despite the brand's affordability and popularity, are actively boycotting Shein.²³ This scenario underscores the profound impact that a company's stance on ethical practices, such as selling vegan products or maintaining ethical business standards, can have on consumers, especially among the younger, socially conscious generation that places a premium on making ethical choices.

¹⁸ '7 Out Of 10 Gen Z Will Keep Being Vegan In The Next 5 Years – Gen Z Is Leading The Veganism Trend, Data Says' (*VEGWORLD Magazine*, 31 March 2022) <<https://vegworldmag.com/7-out-of-10-gen-z-will-keep-being-vegan-in-the-next-5-years-gen-z-is-leading-the-veganism-trend-data-says/>> Accessed 12 Feb. 2024.

¹⁹ *Ibid.*

²⁰ Neiman Marcus and others, 'Join Growing List of Fashion Brands That Are Anti-Fur' (*Peoplemagazine* 30 June, 2021) <<https://people.com/style/fur-free-luxury-fashion-brands/>> Accessed 12 Feb. 2024.

²¹ Thuy Le, 'vegan trend in consumer buying behaviour' (Bachelor's thesis, Oulu University of Applied Sciences 2019).

²² 'Shein Has Lost a Third of Its Market Value' (*Nss Magazine*, 02 February, 2023) <<https://www.nssmag.com/en/article/32102>> Accessed 13 Feb. 2024.

²³ Eden Havel, 'Why Are People Boycotting Shein?' *Triton Times* (13 January, 2023) <<https://tritontimes.com/48411/columns/why-are-people-boycotting-shein/>> Accessed 13 Feb. 2024.

Reputation and Social Risk

The interconnection between reputational risk and social risk holds significant weight, particularly within today's digital realm where social media wields considerable influence. According to the World Economic Forum, over a quarter of a company's market value can be directly linked to its reputation, a figure underscored by recent events highlighting the profound repercussions of poor decision-making on financial standings.²⁴ With information and opinions swiftly circulating across diverse online channels, the repercussions of reputational risks can prove calamitous for companies and their stakeholders. Thus, companies are justified in devoting increased focus to nurturing the components that shape their corporate reputation.

On the contrary, companies that fail to address social equity concerns expose themselves to heightened risks of reputational harm. Without proactive steps to tackle social risks, these companies run the peril of damaging their brand perception, eroding consumer trust, and enduring public scrutiny, all of which can deeply impact their long-term market viability and sustainability.²⁵ Hence, effectively managing social risks emerges as a vital aspect of safeguarding and enriching a company's reputation, highlighting the importance of prioritizing ethical and socially responsible business practices and taking a stand on social issues in today's corporate landscape. At times, corporations may find themselves entangled in complex social dynamics such as where they are compelled to yield to widespread consumer protests to safeguard their reputation for broader financial interests.²⁶ The increasing prevalence of social media, particularly among younger demographics, underscores the significance of companies upholding their image in public discourse.²⁷ These arguments can be demonstrated with the help of case studies.

Starting with the case of Shein, the company's reputation suffered due to various factors, including numerous videos circulating over social media highlighting the poor quality of its garments, as well as political activism from environmental groups condemning the practices of

²⁴ 'Corporate Brand Reputation outranks financial performance as most important measure of success' (3 BL CSR Wire, 1 April, 2024) <https://www.csrwire.com/press_releases/21696-corporate-brand-reputation-outranks-financial-performance-as-most-important-measure-of-success> Accessed 13 Feb. 2024.

²⁵ Wole Segun, 'ESG Social Risks Overview' (*AuditBoard*, 19 October, 2023) <<https://www.auditboard.com/blog/social-risks-esg>> Accessed 14 February 2024.

²⁶ Vlad Demsar and others, 'Calling for Cancellation: Understanding How Markets Are Shaped to Realign With Prevailing Societal Values' (2023) 43(3) *Journal of Macromarketing*, <<https://doi.org/10.1177/02761467231168874>> Accessed 14 February 2024.

²⁷ Divyesh Bhatasana, 'Ethical Social Media Marketing: Balancing Promotion and Responsibility' (*Bulkly* ,26 Jan. 2024) <<https://bulk.ly/ethical-social-media-marketing/>> Accessed 14 February 2024.

fast fashion and educating younger generations about its detrimental impact on the environment.²⁸ Shein's attempts to improve its reputation seem futile, as the brand's unethical practices are deeply ingrained in public perception resulting in substantial loss in consumer base. Additionally, in the context of the Russia-Ukraine conflict, several companies have either downsized or exited the Russian market, citing reputational risks among their reasons. For instance, UNIQLO faced significant backlash and a #boycottUNIQLO campaign, leading to the closure of its shops in Russia.²⁹

Similarly, in the Israel-Palestine conflict, boycott campaigns have targeted companies with perceived pro-Israeli stances or financial ties to Israel, with social media serving as a platform for such activism, particularly in regions with security restrictions like Egypt.³⁰ In Jordan, residents supportive of boycott efforts have even entered McDonald's and Starbucks branches to persuade customers to not to enter into transactions with such companies.³¹ To mitigate the damage, Starbucks released a statement emphasizing its non-political stance and refuting rumors about providing support to the Israeli government or military.³² McDonald's faced criticism, particularly in its Israeli franchise, as reports surfaced that it provided free meals to Israeli military personnel, resulting in a significant drop in sales, estimated at least 70%.³³ Furthermore responding to public pressure, Turkey's Parliament removed Coca-Cola and Nestle products from its restaurants, citing a "public outcry" against the brands.³⁴ However, the challenges to a company's reputation work both ways. It's not just companies with economic connections to Israel facing difficulties; the reverse is also true. Shein, a popular clothing giant among the Israeli population, experienced boycotts and backlash in Israel for selling Palestinian

²⁸ Astha Rajvanshi, 'Shein's Massive Popularity Comes at a Huge Cost to Us All' *TIME* (17 January, 2023) <<https://time.com/6247732/shein-climate-change-labor-fashion/>> Accessed 14 February 2024.

²⁹ Kanako Matsuyama, 'Uniqlo Shatters Shops in Russia Days after CEO Said Chain Would Stay Because "Clothing Is a Necessity of Life"'. *Fortune* (10 March, 2022) <<https://fortune.com/2022/03/10/uniqlo-fast-retailing-shatters-shops-russia-ceo-said-chain-would-stay-open/>> Accessed 14 February, 2024.

³⁰ Saafan and others, 'Boycott Campaigns over Gaza War Hit Western Brands in Some Arab Countries' (*Reuters*, 23 November, 2023) <<https://www.reuters.com/business/retail-consumer/boycott-campaigns-over-gaza-war-hit-western-brands-some-arab-countries-2023-11-22/>>, Accessed 15 February, 2024.

³¹ Laura Boushnak, 'Jordanians Boycott American Companies Seen as Pro-Israeli'. *The World from PRX*, (4 December, 2023) <<https://theworld.org/stories/2023-12-04/jordanians-boycott-american-companies-seen-pro-israeli>> Accessed 15 February, 2024.

³² Natalie Shernam, 'Starbucks Blames 'misrepresentation' after Israel Gaza Protests' *BBC News* (20 December, 2023) <<https://www.bbc.com/news/business-67777506>> Accessed 15 February, 2024.

³³ Zachary Folk, 'McDonald's Blames "Misinformation" About Stance On Gaza War For Hurting Middle East Business' *Forbes*, (4 January, 2024) <<https://www.forbes.com/sites/zacharyfolk/2024/01/04/mcdonalds-blames-misinformation-about-stance-on-gaza-war-for-hurting-middle-east-business/>> Accessed 15 February, 2024.

³⁴ Sayantani Biswas, 'Turkey Boycotts Coca-Cola, Nestle from Menu over Alleged Support for Israel'. *Livemint*, (7 November 2023) <<https://www.livemint.com/news/world/turkeys-parliament-removes-coca-cola-and-nestle-products-over-alleged-support-for-israel-in-war-with-hamas-11699364292991.html>> Accessed 15 February, 2024.

flags and canceling sponsorships of Israeli influencers.³⁵

The potential harm to a company's reputation can extend further, possibly resulting in dissatisfied employees and disillusioned customers. In recent times, there has been a growing expectation for businesses to take a stand on political issues, driven by both staff and customers.³⁶ While some corporate leaders express concerns about potential office conflicts and the impact of top-level statements on workplace dynamics, the evolving trend of employees bringing more of their personal lives into professional settings adds an additional layer of complexity.³⁷ For multinational corporations (MNCs) operating globally, expressing a stance on a social issue can be particularly challenging, fostering internal conflicts among employees and executives or triggering tensions between employees in different geopolitical regions. Further, these tensions could possibly lead to labor strikes resulting in scarcity of skilled employees directly affecting productivity and reputation of the company. A striking example is the pushback faced by companies like Mondelez, Nestlé, PepsiCo, and Metro from employees in Ukraine and Eastern Europe, outraged by the firms' decisions to maintain business ties with Russia.³⁸ Another instance involves Starbucks, which recently sued its workers' union, alleging that a pro-Palestinian social media post from a union account stirred controversy among customers and negatively impacted the company's reputation.³⁹

In an era where organizations face unprecedented levels of reputational scrutiny from a diverse and increasingly vital array of stakeholders, as is evident from the above case studies, the concept of subjective norm gains heightened relevance. Subjective norm refers to the perceived social influence on one's decision to engage or abstain from a particular behavior, shaped by encouragement or discouragement from the external environment—spanning family, friends, colleagues, and social media.⁴⁰ The intricate social milieu poses a significant challenge for multinational corporations, requiring deft navigation through conflicting interests among

³⁵ 'Israelis Call to Boycott Shein after Palestinian Flag Scandal' *The Jerusalem Post* (20 October 2023), <<https://www.jpost.com/business-and-innovation/article-769165>> Accessed 15 February, 2024.

³⁶ '#BrandsGetReal: Championing Change in the Age of Social Media' (*Sprout Social*), <<https://sproutsocial.com/insights/data/championing-change-in-the-age-of-social-media/>>, accessed 18 February 2024.

³⁷ Tsedal Neeley, 'Global Teams That Work' (*Harvard Business Review*, 1 October 2015) <<https://hbr.org/2015/10/global-teams-that-work>>, accessed 18 February 2024.

³⁸ Jessica DiNapoli and others, 'Focus: Oreo-Maker, Nestle, Pepsi Face Pressure from European Employees over Russia' (*Reuters*, 14 April, 2022) <<https://www.reuters.com/business/oreo-maker-nestle-pepsi-face-pressure-european-employees-over-russia-2022-04-14/>>, accessed 18 February 2024.

³⁹ Ryan Grim, 'Starbucks Is Suing Its Union After "Solidarity With Palestine!" Tweet', (*The Intercept*, 17 October, 2023) <<https://theintercept.com/2023/10/17/starbucks-suing-union-israel-palestine/>>, accessed 18 February 2024.

⁴⁰ *ibid* 21

national branches, stakeholders, and stockholders. The added layers of complexity arise from potential reputational costs and the imperative to meet quarterly and annual financial reports.⁴¹ As articulated, what resonates positively with one group of stakeholders in a specific region may be received unfavorably by others. However, the caution against insincere communication merely for the sake of it is essential, as employing "bland" public relations material risks alienating diverse groups and generating negative reactions across the board.⁴²

Ethical investing

An additional pivotal aspect that contributes to a comprehensive understanding of the authors' argument is the domain of ethical investing, now commonly referred to as Socially Responsible Investment (SRI). In the context of this paper, "ethical investing" is elucidated as the utilization of nonfinancial normative criteria by investors when selecting securities for their portfolios. The fundamental ethical rationale behind SRI lies in the belief that investment decisions should not be exempt from the ethical scrutiny applied in other facets of life.⁴³ SRI has evolved to exert a substantial influence on financial markets and the broader economy. Its primary objective is to encourage corporate managers to adopt more ethical practices. However, ethical investors, distinct from other investor types interested in normative issues, also seek returns based on the market risk of their investments.⁴⁴ They aspire to influence managers to act more ethically from the investor's perspective, or alternatively, to ensure that managers maintain ethical practices that might be compromised without the backing of ethical investors. The efficacy of ethical investors in fulfilling their duty, including influencing corporate behavior, hinges on the market's reaction to the implementation of more ethical corporate practices.⁴⁵ Investors have the option to conduct individual stock research, rely on recommendations from various groups, or invest in ethical mutual funds offered by numerous investment firms.⁴⁶ Consequently, while exploring information about businesses, it is crucial to present a clear depiction of a company's stance on social issues to investors. This information is deemed a material fact that investors require to make informed decisions on whether to invest, retain, or sell stocks of a particular business. Ethical business practices are posited to yield potential

⁴¹ *ibid* 25

⁴² Sarah Murray, 'When Should Business Take a Stand?' *Financial Times*, (9 March, 2022) <<https://www.ft.com/content/5ceffa36-899a-4457-919f-b70902162f64>>, Accessed 18 February, 2024.

⁴³ Isabelle Girerd-Potin and others, 'Which Dimensions of Social Responsibility Concern Financial Investors?' (2013) 121(4) *Journal of Business Ethics*, <<https://www.jstor.org/stable/42921403>>, Accessed 19 February, 2024.

⁴⁴ Richard Hudson, 'Ethical Investing: Ethical Investors and Managers' (2005) 15(4) *Business Ethics Quarterly*, <<https://www.jstor.org/stable/3857982>> Accessed 19 February, 2024.

⁴⁵ *ibid*.

⁴⁶ *ibid* at 44.

benefits such as increased profits due to heightened employee productivity, enhanced customer loyalty willing to pay premium prices, diligent suppliers ensuring prompt delivery of quality supplies, and supportive communities bolstering the firm's reputation.⁴⁷

Moreover, maintaining a positive public image and adopting an ethical stance on social issues are perceived as risk-mitigating factors by ethical investors, potentially resulting in enhanced returns.⁴⁸ Socially Responsible (SR) companies strategically evade various risks, such as consumer boycotts, employee strikes, environmental penalties, legal prosecutions and fines, and shifts in social and environmental laws and regulations.⁴⁹ The decision of ethical investors to divest substantial sums from companies not aligning with established social standards can amplify the cost of capital for these firms.⁵⁰ This may stem from diminished risk-sharing opportunities among investors or elevated litigation costs arising from claims related to environmental, social issues, or poor corporate governance. The heightened cost of capital may subsequently give rise to an underinvestment challenge for such non-SR firms, deeming them more risky in the eyes of investors. Consequently, investors are likely to demand an additional risk premium when opting to hold non-SR stocks.⁵¹ Furthermore, companies endowed with a commendable reputation and social standing augment their ability to engage in contracts with other entities, being perceived as morally grounded and adept at risk mitigation.⁵² Consequently, companies are urged to divulge information regarding their social standing on pertinent issues that shape public image, providing valuable insights to potential ethical investors and facilitating the decision-making process. Notably, companies associated with social responsibility are believed to unlock market opportunities not readily accessible to those lacking a similar reputation for social responsibility.⁵³

⁴⁷ Russell Sparkes and others, 'The Maturing of Socially Responsible Investment: A Review of the Developing Link with Corporate Social Responsibility.' (2004) 52(1) *Journal of Business Ethics*, <<https://www.jstor.org/stable/25075231>>, Accessed 19 February, 2024.

⁴⁸ Henry L. Petersen, and others, 'Morals or Economics? Institutional Investor Preferences for Corporate Social Responsibility' (2009) *Journal of Business Ethics*, <<https://www.jstor.org/stable/27735221>>, Accessed 19 February, 2024.

⁴⁹ F. Lopez-Arceiz and others, 'The role of corporate governance and transparency in the generation of financial performance in socially responsible companies' (2017) 47 *Spanish Journal of Finance and Accounting*, <<https://www.tandfonline.com/doi/full/10.1080/02102412.2017.1379798>>, Accessed 19 February, 2024.

⁵⁰ Jonas Nilsson, 'Investment with a Conscience: Examining the Impact of Pro-Social Attitudes and Perceived Financial Performance on Socially Responsible Investment Behavior' (2008) 83(2) *Journal of Business Ethics* <<https://www.jstor.org/stable/25482374>>, Accessed 19 February, 2024.

⁵¹ *ibid* 50.

⁵² *ibid*.

⁵³ Luc Renneboog and others, 'Socially Responsible Investments: Institutional Aspects, Performance, and Investor Behavior.'(2008) 32(9) *Journal of Banking & Finance* <<https://doi.org/10.1016/j.jbankfin.2007.12.039>> Accessed 19 February, 2024.

For instance, Company A, with a strong social standing, finds doors open to newer international markets and enhanced financial prospects. Conversely, Company B, previously associated with supplying arms to conflict zones, faces skepticism and reluctance in similar situations. In this hypothetical scenario, it becomes evident that a company's positive social reputation and public image greatly influence its reception in various communities and by governments worldwide. This dynamic is exemplified in the context of the Russia-Ukraine conflict, where companies aligned with Russia or involved in arms trade faced severe repercussions, including being blacklisted by the Ukrainian government and encountering obstacles in conducting business internationally.⁵⁴ Public sentiment also holds sway over corporate decisions, as seen when Turkey's Parliament responded to public outcry by removing products from brands like Coca-Cola and Nestle due to their business dealings with Israel.⁵⁵ Moreover, companies that take ethical stances on social issues garner trust from stakeholders, including investors, who perceive them as transparent and aligned with certain values. This transparency signals competent management to potential investors, encouraging investment. As socially responsible investing (SRI) gains traction among influential investors, social issues inevitably become prominent on corporate agendas.⁵⁶ Shareholders increasingly advocate for SRI policies, compelling companies to take stands on social issues. In essence, the influence of investors compels corporations to align with social and ethical values, reflecting the growing significance of societal concerns in the business landscape.

Concluding remarks

Rather than solely pursuing profits, the most successful companies are propelled by a sense of purpose—an innate desire to address societal needs and contribute to human betterment. While the existing Environmental, Social, and Governance (ESG) criteria primarily focus on limited parameters, the authors argue for broadening the scope. Although less quantifiable than a carbon footprint or governance structure, the 'S' has vast implications for brand credibility, client trust and stakeholder loyalty.⁵⁷

⁵⁴ Stefan Beutelsbacher, 'Ukraine Blacklist: Shaming the companies still doing business with Russia,' *WorldCrunch*, (26 May, 2023) <<https://worldcrunch.com/focus/western-companies-still-in-russia>> Accessed 19 February, 2024.

⁵⁵ *ibid* 34.

⁵⁶ *ibid* 43.

⁵⁷ Anne Landgraf, 'A Deep Dive into the Social Aspect of ESG' (*Conservice ESG*, 13 May 2022) <<https://esg.conservice.com/the-social-aspect-of-esg/>>, Accessed 19 February, 2024.

This expansion should encompass factors like standing on social issues and public opinion, acknowledging their significant impact. Recent geopolitical challenges, including war, sanctions, and a shifting political climate, have underscored the inadequacies of ESG ratings in accurately reflecting the escalating social and governance risks. For example, during Russia's conflict with Ukraine, ESG-labeled funds held at least USD 8.3 billion in Russian assets, and top European Green-labeled funds were found to have stakes in Russian companies.⁵⁸ Notably, corporate decisions to suspend business operations in Russia often followed social media campaigns and threats of consumer boycotts, highlighting the palpable link between public campaigns and corporate decision-making. However, this influence is not accurately gauged in current ESG ratings globally.

A critical limitation of many ESG ratings providers is their reliance on backward-looking data and information, particularly controversies, to formulate scores and ratings for companies and sectors.⁵⁹ This retrospective approach hampers the assessment of the impacts of events or unforeseen crisis, making it challenging to adapt to evolving circumstances. Sustainable finance analysts argue that existing ESG frameworks may not adequately capture relevant factors, especially in situations where traditional measures are ill-equipped to assess the complexities involved.⁶⁰ As a result, there is a pressing need to refine and enhance ESG methodologies, particularly S, which has less literature comparable to the other two, to ensure a more comprehensive and forward-looking evaluation of companies' environmental, social, and governance practices.

⁵⁸ Alastair Marsh and others, 'ESG Funds Had \$8.3 Billion in Russia Assets Right Before War'. *Bloomberg.Com* (8 March, 2022) <<https://www.bloomberg.com/news/articles/2022-03-08/esg-funds-had-8-3-billion-in-russia-assets-right-before-the-war>>, Accessed 19 February, 2024.

⁵⁹ Trevor David, 'ESG Ratings: A Rebuttal of Prevailing Criticisms' (*Sustainalytics.Com*, 12 June, 2019) <<https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/esg-ratings-a-rebuttal-of-prevailing-criticisms>> Accessed 19 February, 2024.

⁶⁰ *ibid.*