VOXEU COLUMN POLITICS AND ECONOMICS

The politicisation of social responsibility

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There is a growing friction between state governments and large asset managers over environmental, social, and governance practices. This column investigates whether institutional investors' voting patterns on socially responsible investing vary according to the political party in control of the state government where a firm is headquartered. It finds that institutional investors are less likely to support such proposals for firms located in Republican-led states, and this reduction is particularly pronounced in recent years. The reduction is also stronger for larger firms, which tend to attract greater political and media scrutiny.

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On 27 March 2024, the Secretary of State of Mississippi issued an order against BlackRock for alleged securities fraud tied to the company's environmental, social, and governance (ESG) investment strategy. The order accused BlackRock of using 'fraudulent and deceptive means' to impose a political agenda on Mississippi residents, signalling the intensifying friction between state governments and large asset managers over ESG practices (Mississippi Secretary of State 2024). This action is not an isolated incident; in recent years, major asset managers like BlackRock have increasingly found themselves at odds with conservative-leaning states, which oppose the broader push for corporate ESG policies. In 2022 and 2023, states such as Florida, Texas, and West Virginia moved to divest state funds from BlackRock and other firms due to concerns over their ESG strategies, which were perceived as threats to industries vital to these states, including oil and gas (Gelles and Tabuchi 2022).

The broader backdrop to these developments is the rising political polarisation in the US, particularly around corporate responsibility on environmental and social issues (Kempf and Tsoutsoura 2018). Institutional investors, who play a critical role in voting on shareholder proposals linked to such concerns, find themselves navigating a highly polarised environment. While Democratic leaders often advocate for corporate engagement with issues like equity, human rights, and environmental sustainability, their Republican counterparts frequently resist such initiatives, criticising them as politicised actions that go beyond the business interests of firms. This divergence places institutional investors in a difficult position as they attempt to balance their fiduciary duties with the political dynamics of the states in which the firms they invest in are headquartered.

In our analysis, we investigate whether institutional investors' voting patterns on environmental and social proposals, broadly categorised as socially responsible investing (SRI) proposals, vary according to the political party in control of the state government where a firm is headquartered. Our findings reveal that institutional investors are less likely to support SRI proposals for firms located in states governed by Republican leaders. This reduction in support is particularly pronounced in recent years, coinciding with the growing polarisation surrounding corporate social responsibility (CSR) and is especially evident among larger institutions and firms that tend to attract more political attention.

There are several plausible reasons why institutional investors may alter their voting behaviour based on state-level political leadership. State governments exert significant influence over firms' operations through policies, tax incentives, and contracts. Politicians can retaliate against firms whose activities conflict with their political priorities, potentially jeopardising a firm's local business interests. Investors, acutely aware of these risks, may hesitate to back SRI initiatives that could antagonise local political leaders. Additionally, institutional investors may aim to avoid drawing the ire of politicians who wield significant influence over state-controlled assets and possess the capacity to generate negative publicity.

To explore the potential influence of state-level politics on investor voting, we analysed an extensive dataset covering institutional investors' votes on every shareholder proposal between January 2006 and June 2021. Our focus on SRI-related proposals stems from consistent polling data indicating that Democratic voters are more likely to prioritise issues such as sustainability, human rights, equity, and political contributions — the very topics these proposals typically address. To ensure robustness, we employed high-dimensional fixed effects, incorporating meeting-level fixed effects to account for firm- and time-specific factors, institution-by-month-by-SRI fixed effects to control for institutions' monthly voting tendencies on SRI proposals, and industry-by-month-by-SRI fixed effects to capture variations in support across industries.

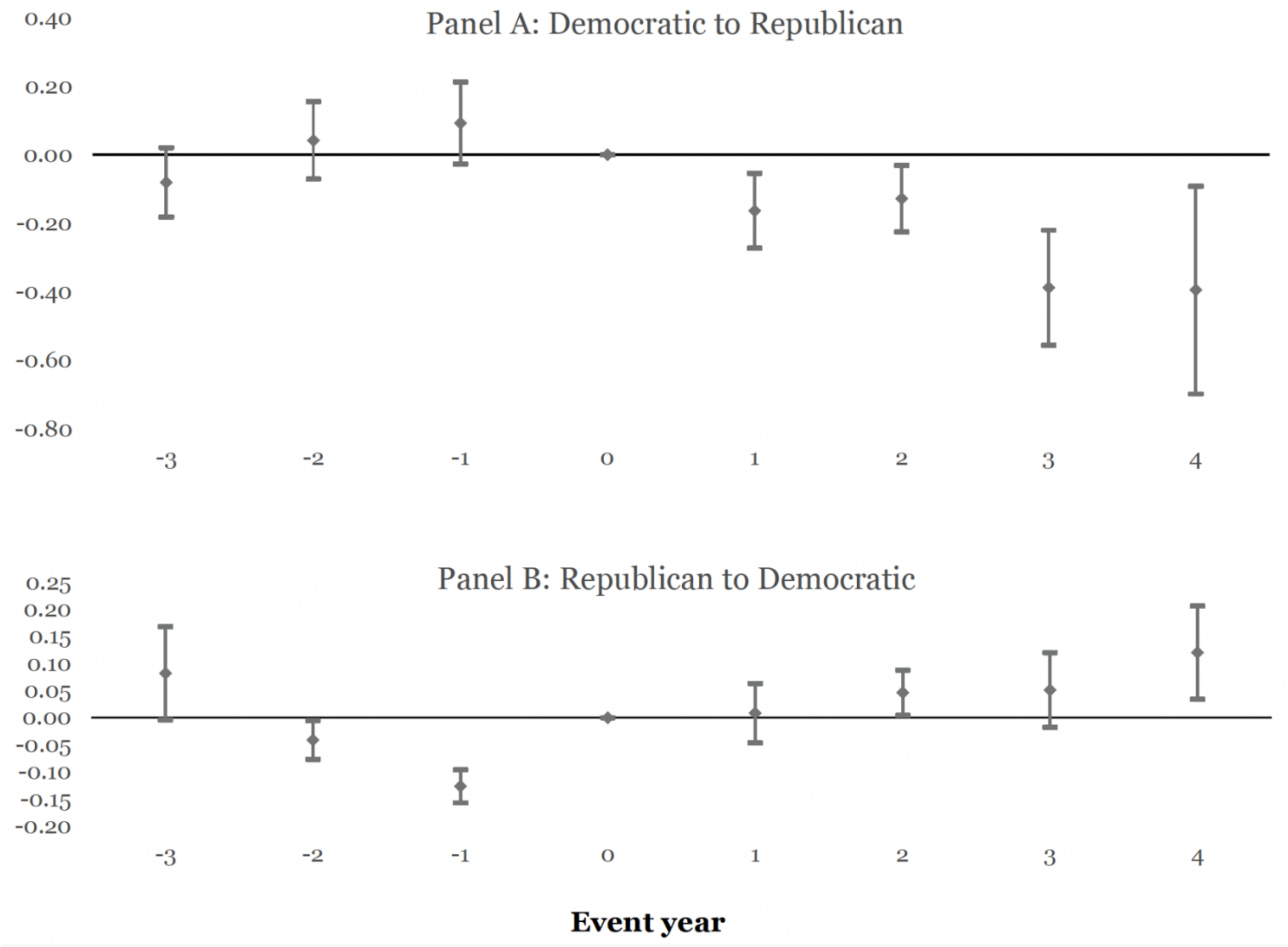
Our core analysis examines whether institutional support for SRI proposals is lower in states with a Republican governor, focusing on governors as they hold significant sway over local firms through appointments, budgetary decisions, and legislative vetoes. Additionally, we conduct robustness tests, including analysing states where one party controls both the governorship and the legislative bodies, as well as using alternative proxies to measure firms' exposure to state politics.

The results of our analysis reveal a strong and statistically significant relationship between state-level politics and institutional voting behaviour. Specifically, institutional support for SRI proposals is 4.1 percentage points lower for firms headquartered in Republican-led states, translating to a 13% decrease compared to the average support across our sample. Notably, this correlation between state-level politics and investor voting has grown more pronounced over time. While the negative association between Republican governorships and SRI support was significant during President Obama's second term (2013-2016), it intensified during the Trump administration (2017-2020). Prior to 2013, the relationship was weaker and lacked statistical significance.

We also observe that the relationship between political leadership and SRI voting is more pronounced for larger firms and institutions, which tend to attract greater political and media scrutiny. Furthermore, the decline in support is especially evident for firms and institutions with substantial media coverage or when the institutional investor holds a significant ownership stake in the firm.

To examine the within-state effects of political leadership changes, we use a stacked triple-difference approach (Gormley and Matsa 2011, 2016). Our findings show that when a state transitions from a Democratic to a Republican governor, institutional support for SRI proposals drops by ten percentage points, corresponding to a 30% reduction relative to the average support level. This shift occurs for both types of political transitions—Democratic to Republican and vice versa. Panel A of the figure illustrates that the relative decline in SRI support in states switching to Republican governors aligns with the timing of the political transition, starting the year after the election and growing more pronounced during the governor's first term. In contrast, the timing of the increase in SRI support following Republican-to-Democrat transitions, as shown in Panel B, is less closely linked to election cycles.

Figure 1 Timing of observed change in within-state socially responsible investing (SRI) support



Our findings also demonstrate that state-level politics influence the likelihood of SRI proposals passing. Approximately 8% of SRI proposals in our sample are within ten percentage points of passage, indicating that the governor's political affiliation could be a key determinant of whether these proposals succeed. Consistently, we find that SRI proposals are 17 percentage points less likely to pass in states with a Republican governor compared to those with a Democrat governor.

Several potential mechanisms may explain how politics influences investor votes. One possibility is that investors adjust their voting behaviour to align with the political preferences of the state's workforce and consumers, thereby avoiding friction between the firm and local stakeholders. Alternatively, investors may be directly concerned with the political influence of newly elected leaders. In support of this latter explanation, we find no evidence that within-state shifts in investor support are smaller when the political transition follows a close election or minor changes in party popularity at the state level.

Investors' motivations for altering their voting behaviour may stem from various factors. One possible explanation is that institutions act in their own self-interest, adjusting their votes to avoid potential retaliation from state politicians. Local politicians may divest state-controlled assets from institutions that support SRI proposals or use their media influence to draw negative attention to the institution's voting stance. Another possibility is that institutions adjust their votes out of fiduciary duty, fearing that pushing a firm to adopt actions counter to local political preferences could result in economic losses if state-level subsidies or tax incentives are withdrawn. While it is difficult to distinguish between these motivations, our evidence suggests that fiduciary duty considerations play a role, particularly in states that allocate a larger share of GDP to business subsidies.

Our research adds to the growing body of literature on the interplay between political partisanship and economic decision-making. Previous studies have shown that political affiliation can influence individual economic choices and corporate behaviour (Gorodnichenko et al. 2020, Engelberg et al. 2023, Meeuwis et al. 2022, Pan et al. 2023). Our paper extends this body of work by demonstrating that external political factors, particularly state-level politics, can also influence shareholders' decisions. The shifts in investor behaviour we observe, which have intensified in recent years, suggest a new and important mechanism through which political polarisation is affecting corporate governance and decision-making.

Finally, our findings have broader implications for firms' corporate social responsibility (CSR) activities. Previous research has highlighted the role of stakeholders, legal frameworks, and judicial decisions in shaping CSR initiatives. For example, Giannetti et al. (2019) argue that investors and customers can impose their social preferences on firms. Our results suggest that firms must also consider the political climate in their home states. When local politicians oppose CSR activities, investor support for such initiatives may wane, presenting an additional hurdle for firms seeking to pursue these goals.

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