Walking the walk? Bank ESG disclosures and home mortgage lending

Do banks with high ESG ratings provide more mortgage loans in poor neighborhoods, or do they engage in social wash by limiting lending in these areas?

This study by Sudipta Basu, Wei Wang, and their colleagues, published in Review of Accounting Studies, investigates the relationship between banks' ESG ratings and their home mortgage lending in poor neighborhoods. The authors find that banks with high ESG scores issue fewer mortgages in disadvantaged areas, measured at both county and census tract levels, even after controlling for bank size, deposit networks, and credit screening. This disparity worsens in disaster-affected areas hit by severe hurricanes and persists across different ESG rating sources.

The paper proposes a social wash hypothesis, suggesting banks use symbolic ESG disclosures to project social responsibility while limiting actual lending in poor communities. Enforcement of the Community Reinvestment Act (CRA) partially mitigates this effect, with banks rated "Outstanding" under CRA reducing the lending gap.

The study also finds that high-ESG banks are more likely to reject mortgage applications in poor neighborhoods but do not charge higher interest rates, indicating the disparity is driven by loan denial rather than pricing.

The authors conclude that ESG disclosures may not fully reflect banks' social contribution through mortgage lending, emphasizing the need for improved ESG rating frameworks and stronger regulatory oversight. The findings highlight ongoing challenges in ensuring equitable credit access and call attention to the limits of current ESG practices in addressing social issues.

MAJOR TAKEAWAYS:

- High-ESG banks lend less in poor neighborhoods despite prosocial ESG disclosures.
- CRA enforcement reduces but does not eliminate the lending disparity linked to ESG ratings.
- Loan denials, not pricing, drive the mortgage lending gap between high- and low-ESG banks.

WHO NEEDS TO KNOW:

- Regulators
- Bank Executives
- ESG Rating Agencies

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