



ALLIANCE UNIVERSITY

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Alliance School of Business

STUDYING THE INFLUENCE OF ESG SCORES ON INVESTMENT DECISIONS

Submitted By:

THARINI S A

Registration No:

2023MMBA01ASB052

Under The Guidance Of:

DR. NUSRATHUNNISA



ALLIANCE UNIVERSITY

Alliance School of Business

Master of Business Administration

DECLARATION

I confirm that this report titled "Studying the influence of ESG scores on investment decisions" truly represents my work undertaken as a part of my dissertation. I certify that this report represents my ideas in my own words and where others' ideas or words have been included, I have adequately cited and referenced the original sources. I also certify that I have adhered to all principles of academic honesty and integrity and have not misrepresented or fabricated or falsified any idea/data/fact/source in my submission. The work has not been submitted to any other Institute for any degree or diploma. I understand that any violation of the above will be caused for disciplinary action by the Institute and can also evoke penal action from the sources which have thus not been properly cited or from whom proper permission has not been taken when needed.

Signature of the Student: *Tharini S. A*

Name of the Student (in Capital Letters): THARINI S A

Registration No: 2023MMBA01ASB052



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CERTIFICATE

This is to certify that Ms. Tharini S A Registration No. 2023MMBA01ASB052 has completed the dissertation titled "Studying the influence of ESG scores on investment decisions " under my guidance as part of the dissertation, serving as partial fulfilment of the requirements for the degree of Master of Business Administration.

Signature of Faculty Guide:

A handwritten signature in black ink, appearing to read "Nusrathunnisa", written over a horizontal line.

Name of the Faculty Guide: Dr. Nusrathunnisa

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CHAPTER 1: INTRODUCTION

The subject of financial research, analysing the impact of ESG scores on the investment decision has received much attention in the recent past, this is because of the changes in investment management that have shifted to sustainable and ethical considerations. ESG factors are new metrics that help the investor determine the sustainability and the level of its ethical appropriateness. This is due to the rising concern of the global issues like climate change, social justice, and governance concerns, which have led investors to put their capital only to the organizations that shall generate value financial, as well as non-financial.

THE EVOLUTION OF ESG CONSIDERATIONS

HISTORICAL CONTEXT:

It can mainly be linked to the SRI that began in the 1960s and the 1970s. The early SRI communicated basically through the negative screening referring to socially objectionable operations such as production of tobacco and arms. Yet, as the world suffered from numerous and rather severe environmental issues and social inequality, the investment community came to a conclusion that they need to embark on the development of a more efficient approach that includes such elements as the process of identifying more acceptable investments with the help of the positive screening process, as well as an active involvement in the ES executives.

EMERGENCE OF ESG METRICS:

The practice of developing ESG metrics started only in the 1990s with the appearance of numerous frameworks and rating agencies that aim to assess corporate actions based on ESG factors. MSCI, Sustainalytics, FTSE and many such more, which designed methods to ascribe numeric rating to businesses according their ESG standards. The scores are also useful for investors when trying to add sustainability into their investment processes. As research in the area advanced through the early years of the new millennium, it became evident that companies with superior ESG scores tended to provide superior returns in the long run, thus offering investors a reason to factor these two elements into their investment decisions.

THE RISE OF ESG METRICS: A NEW PARADIGM:

The practice of developing ESG metrics started only in the 1990s with the appearance of numerous frameworks and rating agencies that aim to assess corporate actions based on ESG factors. MSCI, Sustainalytics, FTSE and many such more, which designed methods to ascribe numeric rating to businesses according their ESG standards. The scores are also useful for investors when trying to add sustainability into their investment processes. As research in the area advanced through the early years of the new millennium, it became evident that companies with superior ESG scores tended to provide superior returns in the long run, thus offering investors a reason to factor these two elements into their investment decisions.

Also, emerging sociopolitical realities mean that new legal environments are also appearing to back up such trends. The EU has initiated tries to increase the comparability of ESG reports and improve the disclosure practices of the rating agencies. It is expected that such regulatory environment will address issues of disparity with close evaluations on ESG by different rating agencies, an aspect that has cause more confusion among investors. Double materiality, which concerns itself with the both financial effects of sustainability issues on companies as well as consequences on the wider society, is assuming centrality as a framework of measurement of company performance.

But in the present time, the impact of ESG scores for investment is more enhanced than ever. A multiplicity of triggers has precipitated this shift, including increasing concern with climate change threats and outcomes, social equity issues, and demands for more an corporate companies' disclosure. Investors are now waking up to the fact that the ESG scores provide useful benchmarks for sustainable business models and durability in the face of changing market conditions.

Beyond this, young generations of investors are pushing this change; the millennials and Gen Z are more willing to invest in sustainable companies.

CHAPTER 2: LITERATURE REVIEW

The use of Environmental, Social, and Governance (ESG) scores as information inputs to investment decisions have emerged as an area of significant interest. To gauge the importance of the ESG scores for the investors, this literature review collates facts collected from the existing studies that tried to analyse the effects of the scores on the investment choices.

The authors of the study, Friede, Busch and Bassen (2015), used over 2000 of scientific papers to generate the connection with ESG factors to firm performance. The authors establish that one indicator is, on average, correlated with another in which the results signify a positive connection between the ESG scores and financial performance. This relationship is relevant for investors; basically, confining ESG factors will lead to superior performances and, therefore, dispositioning investments more favourably towards sustainable organizations.

Eccles, Ioannou, and Serafeim (2014) therefore, advance this stream to establish how corporate sustainability influences practice and returns. Some of them argue that the use of sustainable activities reduces cost besides reputation and credibility from the stake holder resulting in high performance. This not only serves as an evidence that ESG scores is a necessary tool in channelling investment toward firms that are likely to pay back most of their future profits.

Further, and more specifically, the study by Atilgan and Demirtaş (2020) on the emerging markets looked at ESG scores and the effectiveness of such scores it emerged that these scores have a great influence in shaping investment decisions. In their study, they conclude that there is increasing demand of investors in ESG factors, particularly when investing in such regions which symbolizes an increasing interest in RI.

This is important as the threats and opportunities that shape emerging markets which is the main organization focus are different from those shaping the mature economies hence manageable if analysed from sustainability perspective.

MARKET RESILIENCE DURING CRISES:

Gibson and Krueger (2021) thus consider how ESG ratings prognosticate stock market performance specifically in the COVID-19 period. According to their analysis they found out that firm with higher ESG scores perform better in downturn which indicates investor might assume high ESG score as a form of risk management. This discovery is important as it holds the implication that in tumultuous economic times the investors could consider firms with effective sustainability management as a priority.

CHALLENGES IN ESG INTEGRATION:

According to Boffo & Patalano (2020), the main problem with ESG investing is that there are discrepancies with regard to reporting guidelines and little agreement on measures across the board. They highlight the matters that call for a better practice in regards to the meaningful increase in transparency and comparability of ESG information. This kind of challenge may limit the ability of those investing to make the right decisions regarding investment since they

cannot determine the real sustainability of the potentials that exist in different investment opportunities.

The paper by Khan, Serafeim, and Yoon (2016) presents basic evidence for ESG risk factors of corporate sustainability. In return, their work proves that high ESG performance is associated with better financial returns recommending that ESG scores are not just ethics metrics but factors that should be accorded materiality importance when making investment decisions. This the authors note that investors who consider a bucket of material ESG factors stands to gain higher returns hence validating the incorporation of these scores.

In fact, Baker and Nofsinger (2010) explore whether these social responsible equity investments generate positive returns. From their current study, they infer that socially responsible investments may produce returns that are equivalent to traditional investments; therefore, they conclude that the integration of ESG factors reduce returns. This paper adds to the growing discussion about the profitability of ESG investing, arguing that it is possible to factor in the moral compasses of investors combined with the generation of profits.

Statman and Glushkov (2009) consider the global evidence of performance of mutual funds investing with social responsibilities and of finding the result that SRF does not mimic the performance of conventional mutual funds. Their research provides evidence for the idea that investors can get average or better return on their investment while practicing the concept of SRI. It makes perfect sense in the larger ESG investment narrative that posits ESG scores as a useful guide when it comes to investing for both profit and purpose.

Sullivan and Mackenzie (2017) present the topic of ESG integration into investment management from an international perspective. This study shows that it is now evident that institutional investors are gradually waking up to realizing the importance of having the right code regarding investment. For their part, they argue that such approaches as embedding ESG factors will enhance financial performance in the long run as well as depreciate several issues that arise from unsavoury sustainability stories. This will go a long way to suggest that such scores are likely to be used even more in efforts to encourage and direct investments towards sustainable objectives.

Al parsimonious with this line of research, this paper studies the stocks of emerging markets with respect to the impact of ESG ratings by Bennett and O'Neill (2021). Altogether they offer evidence that the high ESG status signals high returns on stocks and consequently the perspective of integrating sustainability by the investors of these markets.

This research establishes the potential of ESG ratings to serve as a competent investment information and performance enhancement in the areas characterised by special economic features. This study has indicated that ESG ratings are a means for supporting a portfolio increase in locations that have an outstanding economic climate.

Hsu and Wang (2021) therefore centre on impacts of ESG disclosure in investments within China. From their studies they observe that ESG transparency influences investors by directing more capital for firms with sound ESG disclosures.

This further supports the rationale that a company's financial comparability does not exist in isolation, and include ESG performance which investors care about, as well as the clarity, with which firms report on sustainability activities, which adds to trust and investment attraction.

Lins, Servaes and Tamayo (2017) conduct a study to test this prediction and the role of corporate social capital and corporate social responsibility for firm performance.

These scholars argue that social capital enhances the ability of a firm to obtain more value from CSR initiatives and consequently post improved financial returns. They show a combination of factors of the ESG approach and the presence in them of factors that may influence investment.

Especially Baker-Medard and Lutz-Bachmann (2022) examine how investors react towards ESG ratings particularly during critical event such as, the COVID-19 pandemic. They discovered that investors make it a habit to invest in high ESG firms during the volatile period since they are viewed as a danger minimization tool. This behaviour leads to the conclusion that such ESG performance can act as a shield against market fluctuations making firms with better scores more appealing for risk adverse investors.

Görge and Schmidpeter (2019) analyse how the ESG criteria affect investments on private equity business. They argue that firms in private equity are quickly adopting ESG factors as crucial aspects of investments. The authors also posit that high ESG standards reduce risk and also improve the value for portfolio companies in the long-run.

It confirms further the new practice when investors in private equity firms believe ESG factor as a foundation for gaining competitive advantage and superior performance.

The research reviewed here is undertaken by Kumar and Singh (2020) wherein authors explore patterns between ESG rating and the returns to stock of the Indian markets. Their research result reveals that firms with high ESG rates have a good performance in stock markets; therefore, investors in emerging markets are slowly opening their eyes towards embracing sustainability. It is important for investors to have even more understanding of these ESG ratings for the purpose of making investment decisions especially in the region that has high economic growth and constantly changing regulation.

Chatterji and Toffel (2010) look at the manner in which firms react to receiving a rating on ESG measures. According to their study, they have realized that firms do change their operations based on ESG ratings with potential impacts on investors' evaluations. The authors emphasize that the firms that received lower ratings may engage in activities that would increase their score, which makes them more appealing to SCI. Such trend shows how firm conduct and investors' anticipation on ESG performance are mutually contingent.

STAKEHOLDER THEORY AND CORPORATE GOVERNANCE:

Porter and Kramer (2006) on the topic of 'Creating Shared Value' talk about the relationship between strategy and competitive advantage with CSR. They note that implementing CSR into the corporate strategy can bring value for business and society. This concept is related with ESG investing since organizations that are able to mitigate impacts of environments and social factors in their operational activities will be perceived as bearing more acceptable risks and therefore gain more investment. In making recommendations relating to this subject, the authors argue that CSR should not be seen as a cost but as a value, which offers the actors considerable prospects for competitive advantage, notably regarding the investors.

A comparison of the reviewed literature establishes that ESG scores have a positive correlation with investment decisions in multiple settings. In private equity, good ESG shows a positive relationship with firm value and reduced risk, though in emerging markets, good ESG has higher future stock performance. Also, investors have placed emphasis on the firms' response to ESG ratings as a way of promoting accountability when seeking investment. The incorporation of stakeholder theory enhances the argument of the benefits of investing in ESG

factors to enhance corporate Governance and long-term success. In total, these works suggest that ESG factors play a central function in determining the approaches to investment management and their efficiency. As the stakeholder starts focusing more on sustainable investments, or investment in companies that balance for and non-financial returns, it becomes imperative to know how these dynamics work. Finally, more research should be done on these relationships, although questions related to standardization and measurement of ESG impacts remain a future research limitation particularly across different sectors.

CHAPTER 3: RESEARCH METHODOLOGY

The purpose of this study is to examine how investment decisions are related to ESG scores. Through the purpose of the conceptual study and the systematic literature review, which will be used in this research, the understanding of the effects of ESG factors on investors, factors that drive the consideration of ESG factors while investing and some of the challenges associated with integrating ESG factors into the investment decision will be achieved.

RESEARCH OBJECTIVES:

- To study the relationship between ESG scores and investor behaviour through a systematic literature review.
- To study the factors that drive investors to consider ESG factors in their investment decisions by doing a conceptual study of existing literature.
- To identify potential challenges and limitations in integrating ESG factors into investment processes, if any, by doing a literature gap analysis about and relating to the topic chosen.

RESEARCH DESIGN:

The focus of the conceptual study will be made on the synthesis and analysis of theoretical works on ESG and investment decisions. The identification of these three ESG components allows the study to focus on assessing the viewpoints of investors and the significance and influence of ESG factors in influencing investments and decision making from the viewpoint of the conceptual models applied within this study.

The systematic literature review aims to include, appraise and combine quantitative research findings and theoretical papers related to ESG scores and investment. The SLR will also give a platform to establish the current state of ESG in investment and where research is scarce or mixed.

SYSTEMATIC LITERATURE REVIEW (SLR):

In general, an SLR will use a systematic procedure to enable it to arrive at accurate results. The papers will still be considered although the papers must present findings on ESG scores, investing decisions, investor behaviour and/or problems associated with the process of ESG integration. Focus will be placed upon the journal articles, conference proceedings, white papers, major Reports and industry consensus that have been published in the last decade. The academic articles to include in the literature review will be sourced social sciences/full-text databases, JSTOR, Scopus, Web of Science, Google Scholar. Search terms will include ESG scores; investment decision making; sustainable investment; ESG integration; investor sentiment and ESG concerns. Recent studies of interest that relate to the set research objectives

and methodologies to achieve the goals and objectives will be sought, and key points about the research objectives, methods, results and conclusion of the various found studies documented on a data extraction form. In systematic quantitative review, this study will also conduct a search for existing gaps that might exist based on some specialists, regions or down ways in methodologically studying the influence of ESG scores on investment strategies.

- All researched papers will be considered depending on the topics regarding ESG scores, investment or investors' actions, or challenges of ESG integration.
- For the purpose of the review, the special focus will be made on the articles from peer-reviewed sources, conference papers, white papers and important industry reports published within the last 10 years. ESG scores, investing decisions, investor behaviour and/or problems connected with the ESG integration.
- Special attention will be paid to articles published in peer-reviewed journals, conference papers, white papers, and major industry reports from the last decade.
- Scholarly articles to be included in the literature review will be retrieved from social sciences/full-text databases like JSTOR, Scopus, Web of Science and Google Scholar.
- Keywords for the search will be “*ESG scores*” “*investment decision-making*” “*sustainable investment*” “*ESG implementation*” “*investor attitude*” and “*ESG issues*”.
- Using a checklist: Key points about research objectives, methods, results and conclusion of each study of interest will be documented using a standardized data extraction form.
- Papers will be classified based on topics of interest: motivations of investors, ESG factors and their classification, ESG investment performance, and approaches to the assessment of ESG performance.
- In quantitative synthesis, this study will also look for research gaps that might exist based on certain specialisms, regions or methodological down ways in researching the effects of ESG scores on investment plans.
- This gap analysis will bring out areas of difficulty, restraint and contradiction in the literature on ESG integration in the investment decision.
- Inclusion and Exclusion Criteria: Peer reviewed articles published within the last ten years will be given preference. Published academic research articles, journals and reviews only on ESG scores, investors' behaviour, and investment performance will be incorporated for the study whereas, papers on irrelevant model, non-refereed articles and earlier studies will not be taken into consideration.

CONCEPTUAL STUDY AND ANALYSIS:

In addition to the above systematic review, a conceptual study will identify the factors that relate to investors' decision to factor ESG considerations into their investment decisions. This will include:

A systematic analysis will be made in relation to the papers included in the review to define the main themes of the decision of investors, including the ethical component, financial results, and regulatory impact.

With conceptual frameworks, there will be the ability to explain how the outlined factors relate in order to establish the impact of ESG on investors.

GAP ANALYSIS:

To identify challenges and limitations in integrating ESG factors into investment processes, a literature gap analysis will be performed,

- **Critical Review of Existing Literature:** The literature will be scrutinized to pinpoint gaps related to the challenges faced by investors in adopting ESG criteria.
- **Identification of Limitations:** The analysis will highlight inconsistencies, methodological limitations in existing studies, and areas where further research is needed.

EXPECTED OUTCOMES:

- A deeper understanding of the factors that influence investor behaviour w.r.t ESG.
- Insights into the challenges and opportunities for ESG investing in different markets and sectors.

CHAPTER 4: RESULTS & DISCUSSIONS

By doing a conceptual analysis of the papers studied, we can observe the theories and frameworks and classify the literature gaps in these literatures into three categories.

The three categories of literature gaps are as follows:

1. Methodological Gaps
2. Conceptual Gaps
3. Practical Gaps

THEORIES AND FRAMEWORKS:

- **STAKEHOLDER THEORY:**
The idea of this theory is based on the belief that firms who are accountable to a wider client base, including employees, communities, and regulators through ESG factors may produce superior returns in the long run.
- **RESOURCE-BASED VIEW (RBV):**
ESG performance might also be considered a kind of asset, like brand equity and low operational risk that could impact financial outcomes.
- **MODERN PORTFOLIO THEORY (MPT):**
According to MPT, portfolios with an emphasis on ESG can be associated with lower risk, particularly shifting regulatory frameworks will begin to penalize unsustainable behaviors. The analysis of risks that is not possible when using financial analysis and metrics can be achieved through ESG integration.
- **INSTITUTIONAL THEORY:**
It can help give the external forces—regulatory forces, culture and normative forces—that influence the adoption and success of sustainability strategies in different markets and jurisdictions.
- **DYNAMIC CAPABILITIES FRAMEWORK:**
This theory is an important focus on how firms can create build and transform internal capabilities in relation to variable environments available. Applying this framework to the issue of corporate sustainability might help define how sustainable initiatives change over time as a result of a particular environment.
- **CORPORATE SOCIAL PERFORMANCE (CSP) MODEL:**
The CSP model checks a firm's level of social responsibility and ethical status, a fact that makes its assessment in this study relevant to the sustainability theme. Apparently, incorporating ideas of this model could contribute to defining certain perspectives of sustainability measures and their first- and second-order effects on performance.

- **TRIPLE BOTTOM LINE (TBL) FRAMEWORK:**
This model showing that sustainability will create more positive returns for people, planet, and profit. Applying TBL could enhance the grounds of the conceptual framework providing how social and environmental aspects sustain financial performance.
- **BEHAVIORAL FINANCE:**
This theory, which explores the psychology behind investors' decisions, could enhance understanding of why and how investors weigh ESG factors. Concepts like framing, herding, and risk aversion may influence the perceived importance of ESG scores in emerging markets.
- **RISK MANAGEMENT THEORY:**
The above implies that because firms have complied with ESG standards they stand in a better place to address risks because they are normally likely to evaluate social and environmental risks in the initial instance. This theoretical perspective can justify why ESG rating has been employed in this study as the variable that might contain resource that firms alluded in enhancing their resilience.
- **SIGNALLING THEORY:**
Signalling theory suggests that the information asymmetric assumption means that firms issue ESG ratings to signal the stakeholders about their sustainability and ethicality. Therefore, the ESG ratings during the pandemic can be viewed to some extent as reflecting corporate responsibility hence the stocks in terms of socialised sentiments.
- **SUSTAINABLE FINANCE THEORY:**
Sustainable finance theory, with the critical approach considers that ESG factors are integrated to produce sustainable revenues. With such characteristics, it outlines if there is 'value' in ESG ratings as a way of strengthening the distressed markets' resilience and, whether the resilience was attained throughout COVID-19 pandemic.
- **AGENCY THEORY:**
Examining how corporate governance and executive incentives influence a firm's commitment to material sustainability issues could reveal potential conflicts or synergies in corporate priorities.
- **LEGITIMACY THEORY:**
Legitimacy theory suggests that companies seek to align with societal norms and values to maintain legitimacy. In the context of ESG, this theory can help explain why firms pursue ESG initiatives as a strategy to enhance public perception and sustain legitimacy.

METHODOLOGICAL GAPS:

- **LACK OF STANDARDIZATION IN ESG MEASUREMENT:**

Why the impact that ESG has on investment is highly uncertain is due to the fact that there are many differences in the way that different rating agencies approached ESG scoring. Potential future research could be used to refine the way the ESG issues are quantified: or may explore how different ESG scoring methodologies impact the investment performance.

- **LONGITUDINAL STUDIES:**

Most of the current ESG studies include only cross-sectional data; that is, data are collected only at the end of a particular period. It also implies that annual measures could offer more effective information on how the ESG influences returns with regards to cycles than cross-sectional studies of ESG investments' performance over the following years. Even though the analysed data cover a period of 20 years, which has methodological advantages, the use of longitudinal data can lead to a survivorship bias. This may result in over-estimating the effect of sustainability as firms that have operational sustainable practices are generally more profitable than firms that eventually closed. These findings could lead to over-estimation of the effects of sustainability since only the sustainable firms that continued to operate are incorporated in the study. The analysis covers a specific time period, which might not capture long-term trends in corporate sustainability and their financial impact.

- **COMPARATIVE ANALYSIS OF REGIONAL DIFFERENCES:**

Friede et al. (2015) categorize studies internationally and, therefore, the influence of ESG on the financial performance varies from one region to another due to cultural, legal and economical differences. In the event comparative research is conducted with regards to regional performance on ESG then research might unveil some difficulties or opportunities.

- **CONTROL VARIABLES AND CONFOUNDING FACTORS:**

Despite the use of several control variables in the study, there is also the endogenous variables that might affect results. Due to variations in industry, geographical location, and economic environment, it might be challenging to know the process by which sustainability affects processes within an organization.

- **QUANTITATIVE VS. QUALITATIVE ANALYSIS:**

Quantitative research methods are useful in developing correlation, but pattern causal relationship cannot be determined. The use of quantitative analysis could be useful when examining certain activities, exits, and impulses and variations in an organization that may be overlooked in qualitative analysis.

- **CROSS-SECTIONAL COMPARISONS:**

The study contrasts high-sustainability and low-sustainability firms, but more scrutiny of differences or forms of sustainability practices would provide information on which elements of sustainability (ecological, social, management) impact performance most demonstrably. While the studies make a comparison between high-sustainability and low-sustainability firms,

more refined analysis of different levels or a certain kind of sustainability measures would provide more clear understanding of which aspect of sustainability (environmental, social, governance, etc) has most immediate and significant impact on the performance.

- **DATA SCOPE AND SAMPLE SIZE:**

The study focuses on emerging markets but may have a limited number of countries or companies within this classification. Expanding to a broader or different set of emerging markets may reveal differing dynamics in ESG influence.

- **DATA SOURCE LIMITATIONS:**

As the sources of data, the paper mostly employs the ESG ratings published by the public and the stock market performances. What it can potentially neglect is more detailed or organization-specific indicators, some of which can be related to the organization's impact on the environment, customer, employee etc., which may provide additional value.

- **STATIC VS. DYNAMIC ANALYSIS:**

Consequently, ESG rating analysis was carried out at a particular time during the COVID-19 period, which was a cross-sectional study. A study that involves collecting data both before, during and after the pandemic would generate more information that would explain the dynamics of the ESG factors, and their roles in the resilience of value chains of firms.

- **GEOGRAPHICAL FOCUS:**

The study could have focused on one or a few markets only (for example the US or EU markets). More results can be obtained analysing data from a higher number of countries that, therefore, would verify if the consequences observed equally change with the difference in the economic conditions and regulations. Even though the reviewed research includes a vast number of publications, many of them addressed the economies of the USA and European countries primarily. This gap means that there is a research opportunity to compare the effect of ESG across emerging or different economies.

- **MEASUREMENT BIASES:**

SASB data categorizes issues as “material” or “immaterial” based on expert judgments, which might introduce subjective biases. Additional methodologies to assess materiality, like machine learning techniques for sentiment analysis, could reduce reliance on these categorizations.

- **DIVERSITY OF METHODOLOGIES:**

The review also fails to capture more detailed cross-sectional comparison between the different types of methods that are used in ESG studies, for example, qualitative and quantitative methods, experiment based or have a focus on longitudinal data. The future works might leverage the use of methodological triangulation to capture the complexity of the understanding of ESG investing.

- **DATA QUALITY AND STANDARDIZATION:**

One current problem in ESG research is data dissimilarity that makes comparison challenging due to the variation in the quality of data between sources. This gap implies that more future

research is required with a unification of data collection methodologies or a comparison of how data differences influence outcomes in ESG performance.

- **CAUSALITY AND CORRELATION:**

Most studies conducted in ESG are comparative research hence it is often difficult to establish the actual significance of ESG practices to the financial performance of a firm. This methodological gap could be filled by experimental and quasi-experimental designs whereby the causative relationships between the IVs and the DVs are well elucidated.

CONCEPTUAL GAPS:

- **SECTOR-SPECIFIC ANALYSIS:**
While Friede et al. combine results, further research is required to develop more nuanced information about the consequences at the sector level. For instance, ESG factors related to technology, financials, and energy industries are likely to affect the financial outcomes in a different manner because industries have varying concerns and risks.
- **ESG IN SMALL AND MEDIUM ENTERPRISES (SMES):**
Observations draw from extensive investigations with large, listed firms that generate sufficient ESG information. However, the effect of ESG practices on investment has not been well-examined, especially concerning the SMEs' businesses even though these companies make up a large portion of the world's economy.
- **MECHANISMS OF SUSTAINABILITY IMPACT:**
While proved that sustainability has the positive effects and indicated that the concept requires further explanation for the mechanism. For example, the paper proposes that there should be enhanced stakeholder engagement, while improvements in how the stakeholder trust means a higher value creation in terms of financial performance concept might be useful in enhancing the theory.
- **IMPACT ON ORGANIZATIONAL CULTURE:**
High-sustainability firms are expected to focus more on sustainability, but the relationship between sustainability and organizational culture is not well understood yet. Perhaps enlarging the conceptual model with organizational culture could give more information as to how these practices are prosecuted in the day-to-day organization setting.
- **DIFFERENTIATION BETWEEN TYPES OF SUSTAINABILITY:**
Business sustainability means different things and is a catch-all that encompasses dozens of different ESG aspects. Perhaps, defining the roles and effects of each of the sustainability pillars clearly might assist in establishing isolation of the responsibility of each one and the contribution they all make.
- **ROLE OF INSTITUTIONAL CONTEXT:**
This research fails to integrate coherent theoretical perspectives regarding cultural, legal, and economic factors influencing both the implementation and outcomes of sustainability programmes. These appear as the conceptual models on institutional theory or comparative corporate governance might fit this gap.
- **ESG COMPONENTS DISTINCTION:**
The abbreviation ESG stands for Environmental, Social and Governance, but some research considers ESG as one dimensional. Researching E, S, and G components separately might reveal whether and to what extent some factors matter regarding investment decisions.

- **CULTURAL AND REGIONAL VARIABILITY:**

As it has come clear, emerging markets are quite diverse, and the attitudes towards ESG may differ dramatically because the countries are regulated and organized differently, their culture is distinct, and they practice different industries. We cannot be quite sure that the paper will describe these regional peculiarities in detail.

- **INVESTOR TYPE SEGMENTATION:**

ESG score integration is not the same across various investors including institutional investors, other investors, and impact investors since their response is different. Perhaps, division of the investor types could be taken further to generate better understanding.

- **BEHAVIOURAL ASPECTS OF ESG ADOPTION:**

As ESG scores affect investment decisions, its limitation might not involve a behavioural examination of how and why ESG data is implemented, especially psychological factors and ESG bias.

- **ESG RATINGS HOMOGENEITY:**

Some of these ESG ratings employed in the paper are general in application across firms but can bewray imprecise. These ratings are not always aligned with niche industry factors that determine resilience and ESG performance, i.e., oil or gas firms vs technology organizations. It may also be useful to create more detailed adjusted ESG metrics of industries that would provide even more variation.

- **DIFFERENTIATION BETWEEN ESG FACTORS:**

The paper may fail to disaggregate the impacts of individually on the Environmental, Social, and Governance components on the resilience of stock. Studying these components in isolation might provide new information about which parts of ESG are most effective against fluctuations.

- **INVESTOR BEHAVIOR VS. CORPORATE RESILIENCE:**

In this context, one of the possible drawbacks of the paper is the inability to analyze the impact of all ESG components on stock resilience separately. Investigating these components individually might unveil fresh information about which parts of ESG provide the most buffering.

- **DEFINITION OF MATERIALITY IN SUSTAINABILITY:**

The four components of materiality in sustainability are still expanding, and what may be material for some stakeholders may not be so for others. The study employs SASB's framework that may not capture dimensions of materiality relevant to employees, local communities and policymakers.

- **BROADENING SUSTAINABILITY METRICS:**

Literature review relies mainly on financial consequences from material sustainability topics. While the current research is already vast, the idea could be expanded further to identify social

sustainability impact factors such as employees' health, negative impacts on the environment, and community involvement so as to create the model for the sustainable corporate model.

- **INDUSTRY-SPECIFIC VARIABILITY:**

Thus, even though the study classifies industries at a high level of detail, there could be variation within some industries that could not be captured well. For example, the relevance of some sustainability issues varies greatly within the sub-sectors of a broad classification.

- **DEFINITIONAL CONSISTENCY OF ESG COMPONENTS:**

ESG investing currently has no clearly defined components of E, S, G that are agreed on by entities globally. One conceptual issue is the lack of standardized meanings of the concept that have been used since there are significant differences in what different authors have meant when they used the term. The future research could thus focus on outlining general ESG meanings to be used in research practices or on analyzing the consequences of using one or another ESG definition.

- **DIFFERENTIATION BETWEEN ESG AND TRADITIONAL SRI:**

ESG related to socially responsible investing (SRI), meanwhile it is vital to note that they are entirely different as far as the functions and approaches are concerned. Additional conceptual distinction and the framework distinguishing ESG from SRI may help in demarcation of the research area and reinforcements of ESG as an independent field.

- **THEORETICAL UNDERPINNINGS OF ESG:**

As a result, this paper argues that there is a need to raise the level of theoretical development of ESG research has been noted as most of the work in this field have not been developed on the basis of clearly defined theory. Alternatively, ESG is thought to be made sense of by adopting theories like stakeholder theory, resource-based view, or legitimacy theory.

PRACTICAL GAPS:

- **INVESTOR PERCEPTION AND BEHAVIOUR:**

This is even though there is evidence that indicates ESG improves performance, little is known about how investor attitude towards ESG differs in real-life scenarios. As for the further research, other research could investigate how various kinds of investors (such as institutional investors and small retail investors) take ESG scores into account.

- **IMPACT OF ESG CONTROVERSIES:**

There is scant literature on negative ESG events (e.g., environmental scandals, governance failures) and their impact on the returns on the investment. Knowing how investors behave when exposed to ESG controversies and consequence on the long-term performance can go a long way in revealing the risk management contribution of ESG.

- **SCALABILITY AND APPLICABILITY:**

The paper lacks a clear explanation of how SMEs could adopt sustainable strategies since the study is mainly based on big firms particularly those with a public face. Further research on scalability of the resources available to the external parties for firms with limited resources would help in generalising the findings. The paper does not focus on the issues of creating ESG scores' uniformity across the emerging markets because of their non homogeneity and weak-pinned legal requirements.

- **GUIDANCE FOR IMPLEMENTATION:**

While the paper focuses on the positive impacts of sustainability, it does not offer much information on where or how companies can begin to implement or improve the sustainability in their organizations co-efficient.

- **CONTEXT-SPECIFIC OUTCOMES:**

The tangible benefits of sustainability implementation may significantly differ across industries that warrants one's concerns given that the paper lacks differentiated data by industries. More focused research could again contribute value for different industries which have different requirements and financial capabilities for example manufacturing /tech industries.

- **APPLICABILITY IN VARYING MARKET CONDITIONS:**

Emerging markets are characterised by high volatility and therefore any information used in their evaluation might also be subject to volatility hence not very stable. In the unstable markets, this variability may reduce the possibilities of the effective use of the findings derived from the experimental data.

- **IMPACT ON PORTFOLIO PERFORMANCE:**

The study may also have missed some of the applied considerations to do with portfolios, performance evaluation, which is important to the fund managers that are using ESG factors in the risk-return analysis.

- **REGULATORY CONSTRAINTS:**

It is seen that emerging markets are at differing degrees of regulatory support towards ESG at the current moment. This research might not discuss interaction or constraints by the regulatory organizations on the ESG-based investment practices in these markets. Nonetheless, the study implicitly indicates that material sustainability topics are topics that companies should address but it fails to explain how such behaviour might be encouraged by regulatory bodies. Further research could be done on policy that governments could implement in order to support sustainable practices.

- **LACK OF ACTIONABLE INSIGHTS FOR PORTFOLIO MANAGERS:**

Portfolio managers may require more guidance on how to apply ESG ratings when formulating a portfolio with a view to reducing risk. It is therefore possible to narrow this gap through coming up with practical guidelines on how to incorporate ESG data dynamically in the event of a crisis.

- **IMPACT OF ESG RATINGS VARIABILITY:**

Different ESG ratings exist that vary between the providing agencies and, consequently, may have different meanings. This study could become more utilitarian if a comparative analysis of these differences and impacts on investor's decision-making process was conducted, especially in the periods of crises.

- **SHORT-TERM VS. LONG-TERM IMPACTS:**

The pandemic is a short-term shock, and perhaps the ESG ratings can behave differently in longer, less abrupt market conditions. It would be useful to consider whether ESG works effectively as an anti-risk tool in the short and the long term.

- **APPLICATION FOR SMALL AND MEDIUM ENTERPRISES (SMES):**

The study is predominantly conducted on a large firm sample that is taken from the population of publicly held organizations. While the study was limited to large firms, extending it to SMEs might produce valuable recommendations for organizations of all sizes.

- **INVESTOR COMMUNICATION:**

The conclusion is thus significant to understanding corporate sustainability while not providing guidelines to how firms should disclose information on sustainability activities to the investors. Studying effective practices in communication could be beneficial when trying to achieve the goal of reconciling investor and corporate sustainable agendas.

CHAPTER 5: CONCLUSION

In conclusion, this conceptual study on "Studying the Influence of ESG Scores on Investment Decisions" highlights the multifaceted nature of Environmental, Social, and Governance (ESG) considerations in shaping modern investment paradigms. The integration of various theories and frameworks—from Stakeholder Theory to Legitimacy Theory—illustrates the profound impact of ESG factors on not only financial performance but also on broader societal and environmental outcomes.

KEY TAKEAWAYS:

- **HOLISTIC ACCOUNTABILITY:**
Stakeholder Theory lays the priority for managers in responsibility to multiple stakeholders, and it provides evidence stating that companies focused on ESG criteria are beneficial in terms of higher long-term returns. This goes hand in hand with the concept that has been realized by investors in equal measure where sustainability creates profitability in businesses.
- **RESOURCE AS ASSET:**
The Resource-Based View (RBV) puts ESG performance into focus as a strategic asset like brand equity – aligning with the argument that firms with sound ESG ratings are in a position to manage risks and improve financial outcomes.
- **RISK MITIGATION:**
Indeed, MPT and Risk Management Theory also conveys that ESG-focused portfolios can reduce the risks involved in the investment portfolios as the regulatory measures unfolds and crackdown unsustainable practices.
- **DYNAMIC ADAPTABILITY:**
The Dynamic Capabilities Framework shows how firms can employ constant change and innovation to sustainable initiatives according to environmental contexts to support the discussion highlighting the role of dynamism in achieving sustainability objectives in the long-run.
- **BEHAVIOURAL CONSIDERATIONS:**
Behavioural Finance introduces psychological factors and demonstrates that investor attitudes towards ESG factors switched by the human mind contain biases and affective states, which have a great impact on investment decisions in emerging markets.
- **SIGNALLING AND LEGITIMACY:**
Combined, Signalling Theory and Legitimacy Theory explain how firms use ESG ratings to convey their responsibility and good intention to do business ethically in a society with the hope of gaining recognition from the public.

After exploring how ESG scores affect investing, it is clear that this particular field has a great deal of complexity and opportunity for future growth. This conceptual work has already highlighted many methodological, conceptual and practical gaps that may serve as stimulating paths for future research. For one, a lack of standardization when it comes to ESG measurement methodologies has spawned great uncertainty due to differing scoring methods among rating agencies leading to vastly different results. Consequently, it creates challenges in comparisons and casting shadows on the legitimacy of ESG data as a meaningful driver for investment decisions. Hence, future explorations could either refine the methods of ESG scoring and/or its implications on investment performance creating a data that is more accurate, comparable and actionable.

As the distinction between ESG and traditional socially responsible investing (SRI) remains conceptually fuzzy, we argue theoretically that this is problematic. Furthermore, ESG is even treated as a unit—ESG by the numbers for example—but perhaps each component considered independently could shed a more granular light on how they uniquely influence investment decisions. The variation in ESG impact by industry and region also points to the necessity for context-specific research to understand the role of ESG across markets and sectors.

In practice, investors' attitudes towards ESG is needed to be explored. And since not all investors have the same goals (for instance, institutional investors might care less about people or planet than retail or impact investors), ESG can fall short as a broadly applicable framework. Moreover, examining the impact of ESG controversies & ratings uncertainty on crisis-level investment behaviours is important for understanding the contribution of ESG to portfolio stability and risk management during those crisis periods.

ESG factors are holding more ground as a rightful disruptive force for good in investment landscapes across the world; however there is still a long way to go in our understanding of their actual level of influence on such decisions.

By addressing these gaps, future studies can contribute to a clearer, more consistent, and practically applicable understanding of ESG's influence on financial performance. Ultimately, a standardized, theoretically sound, and empirically validated approach to ESG investing can enhance its utility as a tool for both risk management and value creation, guiding investors toward more informed and impactful decisions in the pursuit of sustainable finance.

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