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Impact of Environmental, Social, And Governance (ESG) Performance On Corporate Financial Performance: A Study from Indian Listed Companies

Dr. P. Srinivasa Reddy

Sr. Asst. Professor
Department of Commerce, Osmania University.
Nizam College, Basheerbagh, Hyderabad - 500001, Telangana.

Abstract

Environmental, Social, and Governance (ESG) performance has become an important consideration in corporate decision-making and investment strategies worldwide. In India, the implementation of mandatory ESG disclosures through the Securities and Exchange Board of India (SEBI) has encouraged listed companies to integrate sustainability practices into their business operations. However, empirical evidence regarding the financial consequences of ESG adoption remains inconclusive, particularly in emerging markets. This study investigates whether corporate financial performance changed following the ESG disclosure period and whether firms with stronger ESG performance demonstrate superior financial outcomes. The study uses a balanced sample of 82 Indian listed companies covering the period from 2018 to 2025. Financial performance is evaluated using Return on Assets (ROA), Return on Equity (ROE), and Tobin's Q, while ESG performance is measured using CRISIL ESG Combined Scores. Paired sample t-tests are employed to compare pre-ESG (2018–2021) and post-ESG (2022–2025) financial performance. The findings reveal that although average ROA and ROE improved after ESG disclosure, the changes are not statistically significant. However, firms with stronger ESG performance exhibit significantly higher ROE and market valuation than firms with relatively weaker ESG performance. The results further indicate considerable variation in financial performance even among firms belonging to the same ESG category, suggesting that ESG performance alone does not guarantee superior short-term financial outcomes. The study concludes that ESG functions as a strategic long-term value creation mechanism rather than an immediate driver of profitability. These findings provide useful insights for corporate managers, investors, and policymakers regarding the evolving role of ESG in the Indian corporate sector.

Keywords: Environmental, Social and Governance (ESG), Corporate Financial Performance, Return on Assets, Return on Equity, Tobin's Q, Composite Performance Index, Indian Listed Companies.

1. Introduction

Environmental, Social, and Governance (ESG) practices have become one of the most influential developments in corporate governance and sustainable business management during the past decade. Investors, regulators, governments, and other stakeholders increasingly expect companies to create value not only through financial performance but also through responsible environmental practices, social accountability, and effective corporate governance. As a result, ESG has emerged as an important criterion for evaluating corporate sustainability, investment quality, and long-term business performance.

The growing importance of ESG is reflected in the rapid expansion of sustainable investment across global financial markets. Institutional investors now consider ESG information alongside traditional financial indicators while making investment decisions. Companies with stronger ESG performance are generally expected to experience lower business risk, improved stakeholder confidence, enhanced operational efficiency, easier access to capital, and stronger corporate reputation. Consequently, many firms have incorporated ESG principles into their strategic planning and business operations.

In India, ESG reporting has gained considerable importance following regulatory initiatives introduced by the Securities and Exchange Board of India (SEBI). The introduction of the Business Responsibility and Sustainability Reporting (BRSR) framework has significantly improved the quality and consistency of sustainability disclosures among listed companies. Mandatory ESG reporting has encouraged firms to disclose information regarding environmental management, employee welfare, corporate governance practices, diversity, stakeholder engagement, and ethical business conduct. These developments have strengthened transparency and accountability while supporting India's commitment towards sustainable economic development.

Despite increasing ESG adoption, the relationship between ESG performance and corporate financial performance remains one of the most debated issues in finance and corporate governance literature. While several international studies report that firms with better ESG practices generate higher profitability and market valuation, other studies find weak, insignificant, or even negative relationships. Such inconsistent findings indicate that ESG investments may produce benefits over different time horizons and across different institutional environments.

The Indian corporate sector provides an interesting context for examining this relationship because ESG reporting has only recently become standardized through regulatory reforms. Since ESG disclosures became more comprehensive after the implementation of the BRSR framework, it is important to examine whether corporate financial performance has improved following the ESG disclosure period and whether firms with higher ESG performance actually achieve better financial outcomes than firms with relatively lower ESG performance.

2. Review of Literature

The relationship between Environmental, Social, and Governance (ESG) performance and corporate financial performance has attracted considerable attention from researchers, practitioners, investors, and policymakers. Earlier research primarily focused on Corporate Social Responsibility (CSR), whereas recent studies have adopted ESG as a broader framework for evaluating corporate sustainability and responsible business practices.

Saini et al. (2023) systematically reviewed empirical studies investigating ESG and financial variables across different countries and industries. Their findings indicated that governance consistently demonstrates the strongest positive association with financial performance, while environmental and social dimensions produce mixed results depending on industry characteristics and institutional environments. The review emphasized that methodological differences largely explain the inconsistent empirical findings reported in previous studies.

Mishra, Datta, and Behera (2024) reviewed corporate environmental responsibility and financial performance in India. The study reported that firms adopting stronger environmental management practices generally improve operational efficiency, reduce regulatory risk, and strengthen stakeholder relationships. However, the authors noted that the financial benefits of environmental initiatives often emerge gradually because sustainability investments involve significant implementation costs during the initial stages.

Li et al. (2024) conducted a systematic literature review examining the influence of ESG performance on firm value. The review concluded that ESG contributes positively to corporate success by improving investor confidence, strengthening corporate governance, enhancing reputation, and reducing business risk. The authors also observed that governance practices exhibit the strongest and most consistent influence on firm value across both developed and emerging economies.

Yap, Leow, and Ismail (2024) reviewed recent developments in ESG finance and concluded that integrating ESG into financial decision-making enhances investment quality, promotes innovation, strengthens proactive risk management, and contributes to sustainable shareholder value. The study further emphasized that ESG has evolved from a voluntary corporate initiative into a strategic component of long-term corporate finance.

Zheng et al. (2025) conducted a bibliometric review and meta-analysis of 140 studies investigating ESG performance and financial stability. Their findings demonstrated that stronger ESG performance generally improves financial stability by reducing corporate risk, strengthening stakeholder confidence, and enhancing governance quality. The study also highlighted the increasing importance of ESG disclosures for investors and financial institutions when evaluating corporate sustainability.

Kim et al. (2026) reviewed recent ESG research published during 2020–2024 and observed that global regulatory reforms—including mandatory sustainability reporting standards—have significantly strengthened the integration of ESG into corporate strategy. The review concluded that recent empirical studies increasingly support the positive contribution of ESG to long-term corporate resilience and sustainable value creation, while also emphasizing the need for standardized reporting frameworks and comparable ESG measurements.

Saxena and Begde (2026) conducted a bibliometric, thematic, and meta-analytical synthesis of 1,128 ESG studies indexed in Scopus. Their meta-analysis confirmed an overall positive relationship between ESG performance and corporate financial performance. However, the authors emphasized that the strength of this relationship varies across industries, firm characteristics, governance quality, and national institutional environments. They recommended that future empirical studies focus on firm-level heterogeneity and emerging markets where ESG reporting frameworks continue to evolve.

3. Research Gap

Although numerous studies have examined the relationship between ESG performance and corporate financial performance, several important research gaps remain.

Most previous studies investigate the relationship using cross-sectional or panel regression models without examining whether corporate financial performance changes following the introduction of mandatory ESG disclosure requirements. Consequently, limited empirical evidence exists regarding the actual financial impact of ESG disclosure over time. existing research generally treats ESG scores as continuous variables while paying relatively little attention to financial performance differences across ESG performance categories. Analysing firms according to ESG classifications enables a more meaningful assessment of whether stronger ESG performance consistently translates into superior financial outcomes. The present study addresses these research gaps by comparing financial performance before and after the ESG disclosure period, examining performance differences across ESG categories, and constructing a Composite Performance Index using ROA, ROE, and Tobin's Q. The findings contribute to the growing body of ESG literature by providing recent evidence from the Indian corporate sector.

4. Research Objectives

The present study aims to achieve the following objectives:

1. To examine whether corporate financial performance significantly changed between the pre-ESG (2018–2021) and post-ESG (2022–2025) periods.
2. To analyse whether firms with different ESG performance categories exhibit significant differences in post-ESG financial performance.
3. To examine the relationship between ESG performance and corporate financial performance using accounting-based and market-based indicators.

5. Research Hypotheses

The study tests six null hypotheses.

H_{01}: There is no significant difference in the mean ROA between the pre-ESG and post-ESG periods.
H_{02}: There is no significant difference in the mean ROE between the pre-ESG and post-ESG periods.
H_{03}: There is no significant difference in the mean Tobin's Q between the pre-ESG and post-ESG periods.
H_{04}: There is no significant difference in post-ESG ROA among ESG performance categories.
H_{05}: There is no significant difference in post-ESG ROE among ESG performance categories.
H_{06}: There is no significant difference in post-ESG Tobin's Q among ESG performance categories.

6. Research Methodology

6.1 Research Design

The present study adopts a **quantitative research design** to examine the relationship between Environmental, Social, and Governance (ESG) performance and corporate financial performance among Indian listed companies. A quantitative approach is appropriate because it enables objective measurement of financial performance and facilitates statistical testing of hypotheses using firm-level financial data.
The study combines accounting-based measures (Return on Assets and Return on Equity) with a market-based measure (Tobin's Q) to provide a comprehensive assessment of corporate financial performance.

6.2 Nature of the Study

The study is Empirical in nature Descriptive and analytical. The empirical component evaluates financial performance using actual financial statements and ESG scores.

6.3 Data Source

The study is entirely based on **secondary data** collected from reliable public sources.
The major sources include:

- CRISIL ESG Reports (Combined ESG Scores)
- Annual Reports of Companies
- NSE India
- BSE India
- Capita line Database
- Money control
- Company Sustainability Reports

The financial statements were cross-verified using multiple sources to improve data reliability.

6.4 Sample Selection

The study focuses on Indian listed companies for which consistent ESG information and financial data are available throughout the study period.
Initially, all companies included in the CRISIL ESG database were considered. After eliminating firms with incomplete ESG scores, missing financial information, mergers, delisting, and inconsistent reporting periods, the final sample consists of 82 listed companies.

6.5 Period of the Study

The study covers the financial years:

2018–2025

For analytical purposes, the study period is divided into two phases.

Pre-ESG Period

2018–2021
This period represents the years before widespread mandatory ESG disclosure under SEBI's Business Responsibility and Sustainability Reporting (BRSR) framework.

Post-ESG Period

2022–2025
This period captures the years following mandatory ESG disclosures, during which companies increasingly incorporated sustainability reporting into corporate governance and strategic decision-making.

The division enables assessment of changes in financial performance associated with the ESG disclosure period.

6.6 Variables Used in the Study

The study employs one independent variable and three dependent variables.

Independent Variable

Environmental, Social and Governance (ESG) Performance ESG performance is measured using the CRISIL Combined ESG Score. The ESG score represents the overall sustainability performance of a company by integrating environmental, social, and governance dimensions into a single composite measure.

For analytical purposes, companies are classified into ESG performance categories.

ESG Score	Category
0–40	Weak
41–50	Below Average
51–60	Adequate
61–70	Strong
Above 70	Leadership

This classification facilitates comparison of financial performance across different levels of ESG performance.

Dependent Variables

Corporate financial performance is measured using three widely accepted indicators.

Return on Assets (ROA)

ROA measures the efficiency with which a company utilizes its assets to generate profits.

$$\text{ROA} = \frac{\text{Net Income}}{\text{Total Assets}}$$

Higher ROA indicates more efficient utilization of corporate assets.

Return on Equity (ROE)

ROE measures profitability from shareholders' perspective.

$$\text{ROE} = \frac{\text{Net Income}}{\text{Shareholders}'\text{Equity}}$$

A higher ROE indicates better returns to equity shareholders.

Tobin's Q

Tobin's Q represents market valuation and investor expectations.

$$\text{Tobin}'\text{s Q} = \frac{\text{Market Value of Equity} + \text{Book Value of Debt}}{\text{Book Value of Total Assets}}$$

Values greater than one generally indicate favourable market valuation.

6.7 Statistical Tools Used

The study employs several statistical techniques to analyse the data.

Descriptive Statistics

Descriptive statistics summarize the central tendency and dispersion of financial variables.

The measures include:

- Mean
- Standard deviation
- Minimum
- Maximum

Paired Sample t-Test

The paired sample t-test compares financial performance before and after the ESG disclosure period. The test examines whether changes in ROA, ROE, and Tobin's Q are statistically significant. The paired t-statistic is calculated as

$$t = \frac{\bar{d}}{S_d/\sqrt{n}}$$

were

$\bar{d}$=Mean Difference

S_d=Standard deviation of differences

n=Number of observations

7. RESULTS AND DISCUSSION

Descriptive Analysis of Financial Performance

Before testing the research hypotheses, descriptive statistics are examined to understand the overall pattern of corporate financial performance during the study period. Descriptive analysis provides preliminary insights into changes in profitability and market valuation following the implementation of ESG disclosure requirements.

Table **7.1** presents the mean values of the three financial performance indicators during the pre-ESG and post-ESG periods.

Table 7.1 Comparison of Mean Financial Performance before and after ESG Disclosure

Financial Indicator	Pre-ESG (2018–2021)	Post-ESG (2022–2025)	Change
Return on Assets (ROA)	0.0716	0.0855	+0.0139
Return on Equity (ROE)	1.2654	3.2470	+1.9816
Tobin's Q	0.5725	0.5469	−0.0255

Source: Computed from company financial statements.

The descriptive statistics indicate that the average Return on Assets (ROA) increased from 0.0716 during the pre-ESG period to 0.0855 in the post-ESG period.

Similarly, Return on Equity (ROE) increased substantially from 1.2654 to 3.2470, indicating that firms generated higher returns for shareholders during the post-ESG period. This improvement may be associated with enhanced investor confidence, stronger governance mechanisms, improved risk management, and increased market acceptance of firms adopting sustainability practices.

In contrast, the average value of Tobin's Q declined slightly from 0.5725 to 0.5469. Although the decline is relatively small, it suggests that stock market valuation did not improve uniformly across all firms despite increased ESG disclosures. Investors may require a longer period before fully incorporating ESGrelated information into company valuations. In emerging markets such as India, financial markets are still adapting to sustainability reporting practices, and market participants may continue to place greater emphasis on conventional financial indicators than on ESG disclosures.

Pre–Post ESG Performance Comparison Using Paired Sample t-Test

To evaluate whether corporate financial performance changed significantly following the ESG disclosure period, paired sample t-tests were conducted for each of the three financial performance indicators. Table **7.2** presents the descriptive statistics for the paired sample analysis.

Table 7.2 Paired Sample Statistics

Variable	Pre-ESG Mean	Post-ESG Mean	Standard Deviation (Pre)	Standard Deviation (Post)
ROA	0.0716	0.0855	0.0754	0.0863
ROE	1.2654	3.2470	6.2344	15.2223
Tobin's Q	0.5725	0.5469	0.3743	0.2824

Source: Computed from company financial statements.

The results indicate that both ROA and ROE increased during the post-ESG period, whereas Tobin's Q recorded a marginal decline. Although these changes appear meaningful from a descriptive perspective, statistical testing is required to determine whether they exceed normal random variation.

The paired correlations between the pre-ESG and post-ESG values were also examined. The correlation coefficients are **0.630 for ROA**, **0.967 for ROE**, and **0.758 for Tobin's Q**, all statistically significant at the 1% level. These strong positive correlations indicate considerable persistence in firm performance over time.

The results of the paired sample t-tests are presented in Table **7.3**.

ANOVA Results

Table:- 7.4 ANOVA Results for Financial Performance across ESG Categories

Dependent Variable	Between Group SS	Within Group SS	F-value	Sig.	Decision
ROA	0.042	0.562	1.931	0.131	Accept H_0
ROE	2156.858	16612.263	3.376	0.022	Reject H_0
Tobin's Q	1.016	5.445	4.851	0.004	Reject H_0

Source: Computed using SPSS from annual reports.

The ANOVA results reveal notable differences in the relationship between ESG performance and different dimensions of corporate financial performance.

For **Return on Assets (ROA)**, the calculated F-value of **1.931** is not statistically significant (p = **0.131**). Therefore, the null hypothesis (**H_0**) is accepted, indicating that asset-based profitability does not differ significantly across ESG performance categories.

This finding suggests that companies with stronger ESG scores do not necessarily generate higher returns from their asset base in the short term. Although ESG initiatives may improve operational efficiency, such improvements often require considerable investments in environmental technologies, employee development, governance reforms, and sustainability reporting.

Consequently, firms classified as **Leadership** or **Strong ESG performers** do not automatically outperform firms in lower ESG categories with respect to ROA. Operational efficiency continues to depend on numerous internal factors, including asset utilization, production efficiency, industry characteristics, managerial capability, and capital intensity.

The results indicate that ESG performance alone is insufficient to explain variations in asset-based profitability among Indian listed companies.

Return on Equity (ROE)
Unlike ROA, the ANOVA results for **Return on Equity** demonstrate statistically significant differences among ESG categories. The calculated F-value of **3.376** with a significance level of **0.022** leads to the rejection of $\mathbf{H_0}$.

This finding indicates that firms with different ESG performance levels generate significantly different returns to shareholders.

ROE reflects management's ability to create value for equity investors. Companies with stronger ESG performance generally exhibit better governance structures, greater transparency, stronger stakeholder relationships, and more effective risk management systems. These characteristics improve investor confidence and may enhance shareholder returns over time.

The significant relationship between ESG performance and ROE suggests that shareholders increasingly recognize sustainability-related initiatives when evaluating corporate performance. This observation supports the growing importance of ESG considerations in equity investment decisions.

Tobin's Q
The strongest statistical relationship is observed for **Tobin's Q**, where the F-value of **4.851** is highly significant ($p =$ **0.004**).

Accordingly, $\mathbf{H_0}$ is rejected.

Tobin's Q represents market valuation rather than accounting profitability. It incorporates investor expectations regarding future growth opportunities, corporate reputation, governance quality, innovation capability, and sustainability performance.

Companies demonstrating stronger ESG performance appear to enjoy higher market valuation because investors perceive them as:
- better governed,
- less exposed to regulatory risks,
- more resilient to environmental challenges,

- more attractive to institutional investors,
- and better positioned for long-term value creation.

Unlike accounting measures, market-based indicators rapidly incorporate investor expectations regarding future corporate performance. Consequently, Tobin's Q captures the strategic value of ESG initiatives more effectively than traditional profitability measures.

These findings suggest that although ESG investments may not immediately improve accounting profitability, they positively influence investor perception and market valuation.

8. Key Findings

The major findings are:

- The paired sample t-test showed that ROA and ROE improved slightly after the ESG disclosure period, while Tobin's Q declined marginally. However, these changes were not statistically significant.
- ANOVA results indicated that ESG performance had no significant impact on ROA but significantly influenced ROE and Tobin's Q.
- The findings suggest that ESG investments generate long-term benefits rather than immediate financial gains.
- Market-based measures (Tobin's Q) and shareholder returns (ROE) respond more positively to ESG performance than accounting-based profitability (ROA).
- ESG is an important strategic factor but is not the only determinant of corporate financial performance.

9. Conclusion

The study concludes that ESG performance contributes positively to shareholder returns and market valuation but does not guarantee immediate improvements in accounting profitability. The findings indicate that the financial benefits of ESG initiatives emerge gradually and depend on firm-specific characteristics and strategic implementation. Therefore, ESG should be viewed as a long-term value creation strategy rather than merely a regulatory compliance requirement.

10. Policy Implications

The findings suggest that regulators should strengthen ESG disclosure standards to improve transparency, comparability, and investor confidence. Policymakers may also encourage wider ESG adoption through appropriate incentives and standardized reporting frameworks.

11. Practical Implications for Investors

Investors should evaluate ESG performance together with traditional financial indicators while making investment decisions. Strong ESG performance reflects better governance, lower risk, and improved long-term sustainability, making it an important consideration for long-term investment strategies.

12. Limitations of the Study

- The study is limited to 82 Indian listed companies.
- ESG performance is measured only using CRISIL ESG scores.

- The post-ESG period (2022–2025) is relatively short.
- Only ROA, ROE, and Tobin's Q were used to measure financial performance.
- Industry-specific differences were not examined separately.

13. Directions for Future Research

Future studies may:

- Examine a longer post-ESG period.
- Conduct industry-wise and cross-country comparisons.
- Analyze Environmental, Social, and Governance dimensions separately.

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