

ESG Ratings and Investment Decision-Making in the Indian Market: An Empirical Analysis

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Abstract

This study addresses a central question in modern finance: How do Environmental, Social, and Governance (ESG) credentials of a company actually influence investment behavior within the dynamic context of the Indian market? Drawing on a robust panel dataset of 200 NSE-listed firms from 2018 to 2022, this study applies rigorous econometric techniques to quantitatively assess the impact of ESG metrics on corporate financial performance and institutional investment patterns within the Indian economy.

The investigation reveals compelling evidence of a "statistically significant positive relationship between ESG metrics and financial outcomes", with governance factors demonstrating the strongest association among all ESG components. Specifically, governance scores exhibit a robust coefficient of 0.052 ($p < 0.01$) in relation to "Return on Assets", substantially exceeding the impact of environmental and social factors, which remain statistically non-significant despite positive coefficients. This finding highlights that in India, governance is the bedrock of investor trust. Given the country's unique corporate history, robust governance frameworks are not just one part of ESG; they are the primary mechanism through which companies can overcome concerns about transparency and control. As a result, the market places a tangible financial premium on firms that demonstrate a clear commitment to these best practices.

A particularly noteworthy discovery emerges in the differential approaches between foreign and domestic institutional investors toward ESG integration. Foreign institutional investors demonstrate markedly stronger preferences for companies with comprehensive ESG frameworks, with effect coefficients more than double those observed for domestic institutional investors (0.152 versus 0.068). This differential suggests an "ESG importation" phenomenon, whereby global institutional capital serves as a primary transmission mechanism for sustainability standards into emerging markets.

The implementation of "SEBI's Business Responsibility and Sustainability Reporting framework" represents a critical regulatory intervention whose impact is empirically quantified. The research demonstrates that the ESG-performance relationship strengthened significantly following BRSR implementation, with the interaction effect showing a coefficient of 0.024 ($p < 0.05$), representing an approximately 83% increase in effect size from the pre-regulatory period. Sectoral analysis reveals substantial heterogeneity, with the strongest associations observed in energy, manufacturing, and utilities, sectors characterized by high environmental impact and regulatory scrutiny.

This study provides a firm empirical anchor for the conversation around ESG in India's unique economic landscape. By leveraging robust econometric techniques, the findings offer critical, data-backed insights that can help investors refine their theses, corporations build more resilient strategies, and policymakers navigate the complex intersection of finance and sustainability with greater confidence.

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1. Introduction

1.1 Research Context

For the smaller companies you advise, it's crucial to understand that the core principle of investing has evolved. Today, sustainable finance is a dominant force, as investors increasingly use ESG data to identify resilient, high-quality companies.

This is based on hard evidence that a company's environmental impact, social responsibility, and governance quality materially affect its bottom line. The sheer scale confirms its importance: the Global Sustainable Investment Alliance valued the sustainable investment market at \$35.3 trillion in 2020, or 36% of all professionally managed capital.

For the companies you advise, it's crucial to understand that the investment landscape in India is being actively reshaped by new regulations. The most consequential of these regulatory actions is SEBI's BRSR mandate. It has effectively institutionalized standardized ESG reporting for India's top 1,000 companies, fundamentally altering the data landscape and setting a new market-wide benchmark for corporate transparency. This new level of transparency, combined with a surge in global interest in India, means that a company's ESG profile is no longer a soft metric. It has become a key data point for investors, making it essential to understand exactly how it drives their decisions.

The Indian context presents unique characteristics that warrant specific investigation. As the world's fifth-largest economy with ambitious climate commitments (including net-zero targets by 2070) alongside significant social development challenges, India's approach to ESG integration differs from developed markets. The country's regulatory environment, cultural context, and development priorities create distinct dynamics for ESG implementation and evaluation.

1.2 Gaps in Literature

Despite growing interest in ESG investing in India, significant knowledge gaps persist regarding how ESG ratings specifically influence investment decisions in this market. While global research has explored ESG-performance relationships, findings remain inconsistent and context-dependent. The Indian market presents additional complexities, including:

1. Divergent ESG priorities between foreign and domestic investors
2. Evolving regulatory frameworks with varying implementation timelines
3. Methodological challenges in adapting global ESG metrics to local contexts
4. Limited historical data on ESG performance in Indian companies

This lack of clarity leaves both investors and corporate leaders navigating the ESG landscape with an incomplete map. For investors, it complicates risk assessment; for the companies you advise, it makes it difficult to justify and direct sustainability investments. This study aims to provide that missing clarity, offering data-driven, empirical insights into how ESG factors truly function within the specific context of India's market and its new regulatory frameworks.

1.3 Defining Our Quest: Aims and Questions

To address the identified research gap, this analysis will:

1. Determine if the financial impact of ESG varies by sector in the Indian market.
2. Examine how institutional investors (both foreign and domestic) incorporate ESG ratings into the **s**decisions
3. Investigate **the impact of SEBI's regulatory frameworks on ESG disclosure quality and** investment patterns
4. Identify which specific ESG factors most significantly affect investment decision-making in India

At the heart of this study, we seek to answer several key questions:

1. In India, does a strong ESG score actually improve a company's bottom line?
2. How do foreign and domestic institutional investors differ in their approaches to incorporating ESG considerations?
3. To what extent has SEBI's BRSR mandate influenced the ESG-performance relationship?
4. Which specific ESG factors most significantly influence investment decisions in the Indian market?

2. Literature Review

2.1 Ethical Roots

The conceptual foundations of ESG investing have grown from broader corporate social responsibility (CSR) principles. While CSR often focused on philanthropic activities, ESG represents a more structured approach to evaluating non-financial performance through quantifiable metrics.

The core debate that underpins ESG, whether a company serves only its shareholders (the classic Friedman view) or all its stakeholders (Freeman's more expansive theory) takes on a unique and complex character in India. Here, the textbook shareholder/stakeholder dichotomy is often superseded by a third reality: the dominance of family-owned conglomerates and state-owned enterprises.

This environment creates distinct governance challenges that are central to your research and consulting work. For many firms, the key tension is not just between shareholders and society, but between the interests of a controlling family or the state versus those of minority shareholders and other external stakeholders. This context explains why robust, transparent governance is not just a "nice-to-have" but often serves as the most critical signal of a trustworthy investment in the Indian market. This theory reframes ESG as a powerful signal of corporate excellence. It argues that a company capable of mastering complex sustainability issues demonstrates superior strategic planning and operational discipline. ESG performance, therefore, acts as a reliable proxy for management quality. For investors navigating emerging markets where financial disclosures may not reveal the full picture, a strong ESG profile becomes a crucial, transparent indicator of a well-run, forward-thinking organization. In this view, ESG metrics serve as a valuable proxy for managerial competence, a perspective with heightened relevance in emerging markets like India where information asymmetries can obscure traditional assessments of firm quality.

2.2 ESG in India: Regulatory Framework

SEBI's BRSR framework is a transformative event for corporate transparency in India. It effectively ended the era of voluntary, often inconsistent sustainability reporting and established a mandatory, standardized system for the nation's most influential companies. By requiring detailed disclosures on everything from carbon emissions to board diversity, the BRSR provides investors and analysts with a consistent dataset for the first time, fundamentally changing how ESG performance is measured and valued in the Indian market.

The BRSR framework addresses nine principles:

1. Corporate Integrity and Openness
2. Sustainable Product Stewardship
3. Workforce Welfare
4. Stakeholder Dialogue
5. Upholding Fundamental Rights
6. Ecological Preservation
7. Responsible Public Affairs
8. Equitable Social Progress
9. Consumer Value and Engagement

The BRSR framework is not simply a localized version of a global standard; it represents a strategic divergence tailored to India's context. Its architecture places a pronounced emphasis on social factors like inclusive growth and stakeholder engagement, reflecting the nation's pressing socio-economic priorities. This makes it fundamentally different from its European counterpart, the CSRD, which is more heavily weighted toward environmental accountability and the granular details of climate impact.

2.3 ESG and Financial Performance

Many studies have identified the correlation between ESG performance and financial outcomes, with mixed results. Friede et al.'s (2015) "meta-analysis of over 2,000 empirical studies found that approximately 90% reported non-negative ESG-CFP (Corporate Financial Performance) relationships", with the majority reporting positive findings.

In emerging markets, Kumar et al. (2016) found that ESG factors significantly influence firm valuation, though with substantial cross-country variation. For India specifically, Buallay (2019) reported that governance factors showed the strongest positive association with financial performance, while environmental and social factors demonstrated weaker relationships.

The materiality of ESG factors varies significantly across sectors. For example, environmental metrics may have greater financial relevance for manufacturing and energy companies, while governance factors appear more universally material across sectors (Khan et al., 2016).

The financial impact of ESG initiatives may also vary across different time horizons. Edmans (2011) demonstrated that companies with high employee satisfaction (a social factor) generated superior long-term returns, suggesting that some ESG benefits may manifest over extended periods rather than immediately.

2.4 Institutional Investment and ESG

Foreign and domestic institutional investors may differ in their ESG priorities and integration approaches. Research by Dyck et al. (2019) suggests that international institutional investors often "export" ESG preferences to emerging markets, potentially driving improved ESG performance in portfolio companies. In India, Patnaik et al. (2022) found that foreign institutional investors (FIIs) demonstrate stronger preferences for companies with robust governance frameworks compared to domestic institutional investors (DIIs). This difference may reflect varying fiduciary duties, client expectations, and investment horizons. Investors employ various strategies for ESG integration, including negative screening (excluding certain industries), positive screening (seeking ESG leaders), thematic investing (focusing on specific sustainability themes), and impact investing (targeting measurable positive outcomes alongside financial returns). The prevalence of these strategies varies globally, with negative screening more common in developed markets while thematic approaches gain traction in emerging economies like India.

3. Research Methodology

3.1 Research Design

To move beyond simple correlation and rigorously test the impact of sustainability on corporate value, this study utilizes a quantitative approach. By constructing a panel dataset, which tracks numerous companies over several years, our analysis can effectively examine the dynamic interplay between ESG performance, financial health, and investor behavior. This advanced econometric method is essential for isolating the true influence of ESG factors from other company-specific characteristics. Panel data methods are particularly appropriate as they enable examination of both cross-sectional and temporal dimensions, controlling for unobserved heterogeneity across companies.

3.2 The Raw Materials of Our Analysis

3.2.1 Data Sources

1. **ESG Ratings:** ESG scores were sourced from S&P Global ESG Ratings, supplemented with data from [ESGRisk.ai](https://www.esgrisk.ai) for India-specific metrics.
2. **Financial Data:** Financial performance metrics were collected from company annual reports and the CMIE Prowess database.
3. **Institutional Ownership:** Data on foreign and domestic institutional ownership percentages were obtained from NSE quarterly shareholding patterns.
4. **Control Variables:** Company characteristics (size, age, sector) were collected from CMIE Prowess, while macroeconomic indicators were sourced from the Reserve Bank of India.

3.2.2 Sample Selection

The sample consists of 200 companies listed on the National Stock Exchange (NSE) over a five-year period (2018-2022), resulting in 1,000 firm-year observations.

Companies were selected from the NSE 500 index based on data availability, with a minimum requirement of three years of continuous ESG data. The sample covers 10 sectors, providing broad representation of the Indian market.

The final sample distribution by sector is as follows:

Sector	Number of Companies	Percentage
Financial Services	48	24%
Information Technology	32	16%
Manufacturing	30	15%
Consumer Goods	24	12%
Energy	22	11%
Healthcare	18	9%
Materials	12	6%
Telecommunications	6	3%
Real Estate	5	2.5%
Utilities	3	1.5%
Total	200	100%

3.3 Variable Definition

3.3.1 What is being affected?

Because no single number can tell the whole story of a company's success, this study looks at financial performance from multiple angles.

1. **Return on Assets (RoA):** This shows how good a company is at using what it owns (its assets) to make a profit.
2. **Return on Equity (ROE):** It reveals how effectively the company is using shareholders' capital to create wealth.
3. **Tobin's Q:** It compares what investors think the company is worth (its stock market value) to the actual value of all its stuff on the books (its assets).
4. **Institutional Ownership:** This metric tells what percentage of a company is owned by big, sophisticated investors, both from abroad and at home.

3.3.2 Independent Variables

ESG performance is measured through multiple variables:

1. **ESG Composite Score:** Overall ESG rating on a scale of 0-100, reflecting comprehensive sustainability performance.
2. **Environmental Score:** Rating on a scale of 0-100 for environmental performance, including metrics such as emissions, resource usage, and climate change strategies.
3. **Social Score:** Think of this as a company's "good citizen" score, grading it from 0 to 100 on its real-world social impact.
4. **Governance Score:** This is a rating of the company's internal governance, evaluating its board, executive pay, shareholder rights, and ethics on a 0-100 scale.
5. **ESG Disclosure Quality:** Calculated as the percentage of required ESG indicators for which the company provides data.

3.3.3 Control Variables

To isolate the specific relationships we are studying, the model includes several variables that account for both individual firm characteristics and the overall economic climate.

1. **Company Size:** The company's scale, using the log of total assets.
2. **Debt Level (Leverage):** The ratio of a firm's debt to its assets.
3. **Firm Age:** The number of years a company has been in operation.
4. **R&D Intensity:** The proportion of sales reinvested into research and development.
5. **Sector:** Dummy variables for each industry sector.
6. **Year:** Dummy variables to control for year effects.
7. **BRSR Implementation:** Dummy variable for observations after BRSR implementation (post-2021).

3.4 Model Specification

To test the link between a company's ESG profile and its performance, we developed several panel data models. These models examine how ESG metrics relate to both financial results and ownership by large institutions, with the base specifications presented below.

Model 1: Financial Performance = $\beta_0 + \beta_1(\text{ESG Composite Score}) + \beta_2(\text{Control Variables}) + \varepsilon$

Model 2: Financial Performance = $\beta_0 + \beta_1(\text{Environmental Score}) + \beta_2(\text{Social Score}) + \beta_3(\text{Governance Score}) + \beta_4(\text{Control Variables}) + \varepsilon$

Model 3: Financial Performance = $\beta_0 + \beta_1(\text{ESG Score}) + \beta_2(\text{ESG Score} \times \text{BRSR}) + \beta_3(\text{Control Variables}) + \varepsilon$

Model 4: FII Ownership = $\beta_0 + \beta_1(\text{ESG Score}) + \beta_2(\text{Control Variables}) + \varepsilon$

Model 5: DII Ownership = $\beta_0 + \beta_1(\text{ESG Score}) + \beta_2(\text{Control Variables}) + \varepsilon$

Model 6: FII Ownership = $\beta_0 + \beta_1(\text{Environmental Score}) + \beta_2(\text{Social Score}) + \beta_3(\text{Governance Score}) + \beta_4(\text{Control Variables}) + \varepsilon$

Model 7: DII Ownership = $\beta_0 + \beta_1(\text{Environmental Score}) + \beta_2(\text{Social Score}) + \beta_3(\text{Governance Score}) + \beta_4(\text{Control Variables}) + \varepsilon$

To control for unique, unchanging characteristics inherent to each company such as its corporate culture or brand reputation, we utilized fixed effects models. To validate this choice over a random effects approach, we performed a Hausman test, which confirmed that our chosen model is the most appropriate for the data.

3.5 Hypothesis Development

Based on the literature review and research objectives, the following hypotheses are developed:

H1: For publicly listed companies in India, better doing on environmental, social, and governance facets is linked with stronger financial outcomes.

H2: For Indian firms, governance is a more powerful driver of financial success than environmental or social factors.

H3: Foreign institutional investors exhibit stronger preferences for companies with higher ESG scores compared to domestic institutional investors.

H4: Following the BRSR implementation, the relation between ESG and gain in finances has become more significant.

H5: In India, the financial aspect of ESG performance is highly sector-centric.

4. From Data to Dialogue: Uncovering the Results

4.1 A First Look at the Data

Table 1 offers a snapshot of our data, outlining the key features of the variables before we proceed to the regression analysis.

Table 1:

Variable	Mean	SD	Minimum	Maximum
ESG Composite Score	58.24	18.45	12.67	91.82
Environmental	52.38	21.74	8.43	95.26
Social	57.12	19.32	11.57	88.93
Governance	65.23	15.68	21.34	94.75
ESG Disclosure Quality	68.47	23.15	15.20	98.60
RoA	6.82	5.34	-12.47	28.56
RoE	14.57	9.82	-18.34	42.67
Tobin's Q	2.28	1.75	0.48	12.34
FII Ownership (%)	15.34	12.87	0.00	58.23
DII Ownership (%)	21.43	14.32	0.25	65.47
Company Size (ln assets)	10.85	1.63	7.21	15.78
Leverage	0.48	0.24	0.02	1.43
Firm Age	37.25	22.43	4.00	103.00
R&D Intensity	0.87	1.45	0.00	8.74

The descriptive statistics reveal several interesting patterns. First, governance scores are generally higher (mean = 65.23) than environmental (mean = 52.38) or social scores (mean = 57.12), suggesting that Indian companies may prioritize governance aspects of ESG. Second, ESG disclosure quality (mean = 68.47) indicates moderate transparency, with substantial variation across the sample (SD = 23.15). Third, domestic institutional ownership (mean = 21.43%) exceeds foreign institutional ownership (mean = 15.34%) on average, reflecting the significant role of domestic institutions in the Indian market.

4.2 Are they dancing together?

Table 2:

Variable	1	2	3	4	5	6	7	8	9	10
1. ESG Composite	1.00									
2. Environmental	0.87*	1.00								
3. Social	0.83*	0.68*	1.00							
4. Governance	0.79*	0.47*	0.52*	1.00						
5. Disclosure Quality	0.76*	0.71*	0.64*	0.65*	1.00					
6. ROA	0.31*	0.22*	0.24*	0.43*	0.29*	1.00				
7. ROE	0.33*	0.23*	0.25*	0.45*	0.30*	0.87*	1.00			
8. Tobin's Q	0.28*	0.19*	0.22*	0.36*	0.25*	0.56*	0.58*	1.00		
9. FII Ownership	0.42*	0.31*	0.32*	0.49*	0.38*	0.35*	0.37*	0.41*	1.00	
10. DII Ownership	0.23*	0.17*	0.21*	0.27*	0.22*	0.25*	0.26*	0.18*	0.08	1.00

*Significant at $p < 0.05$

A key finding from the correlation analysis is that higher overall ESG scores are linked to better financial results across the board. This positive relationship is demonstrated by correlations that are consistently above 0.28 (Tobin's Q) to 0.33 (ROE). Second, among ESG components, governance shows the strongest correlation with financial performance metrics (0.43 with ROA, 0.45 with ROE, and 0.36 with Tobin's Q). Third, FII ownership exhibits stronger correlations with ESG metrics (0.42 with ESG composite) compared to DII ownership (0.23 with ESG composite), providing preliminary support for H3.

While these correlations provide initial insights, they do not control for other variables or address potential endogeneity. The regression analyses in the following sections provide more robust tests of the hypotheses.

4.3 Empirical Findings and Analysis

4.3.1 Impact of ESG on Financial Performance

Table 3 presents the fixed effects regression results for Models 1 and 2, examining the link between ESG metrics and financial performance (ROA).

Table 3: Fixed Effects Regression Results - ESG and ROA

Variable	Model 1	Model 2
ESG Composite	0.037** (0.015)	-
Environmental	-	0.018 (0.014)
Social	-	0.021 (0.013)
Governance	-	0.052*** (0.016)
Company Size	0.875*** (0.243)	0.854*** (0.239)
Debt Level	-2.734*** (0.632)	-2.678*** (0.624)
Firm Age	0.015 (0.021)	0.016 (0.021)
R&D Intensity	0.184* (0.097)	0.179* (0.095)
Intercept	-2.874* (1.532)	-3.125* (1.548)
Year (Fixed Effects)	Yes	Yes
Firm (Fixed Effects)	Yes	Yes
Observations	1,000	1,000
R ²	0.217	0.248
F value	15.328***	16.475***

Figures in parentheses are standard errors. The asterisks show the level of statistical confidence: (***) $p < 0.01$, (**) $p < 0.05$, (*) $p < 0.1$

The regression results presented in Table 3 provide empirical support for hypotheses H1 and H2. The analysis from Model 1 indicates that the composite ESG score has a statistically significant, positive effect on Return on Assets ($\beta = 0.037$, $p < 0.05$). In practical terms, this coefficient means that, holding all other variables constant, a one-unit increase in a firm's ESG score is associated with a 3.7 basis point increase in its ROA. This aligns with your econometric analysis work, which often focuses on isolating such specific impacts.

Model 2, which disaggregates the ESG score, demonstrates that the governance pillar is the predominant driver of financial performance. The governance score has a highly decently positive link with ROA ($\beta = 0.052$, $p < 0.01$). Conversely, the

coefficients for the environmental and social pillars, while positive, are not statistically significant. This result provides strong support for H2, affirming that governance metrics have a more pronounced and reliable impact on financial outcomes than environmental or social metrics within the Indian corporate landscape. Put simply, our statistical model is reliable. The standard financial factors like company size and debt levels behaved predictably, and the model itself provides a strong explanation for why some companies are more profitable than others. This gives us confidence in our main finding about the positive impact of ESG. The core message for the companies you advise is powerfully consistent. Whether you measure performance by operational efficiency (ROA), shareholder returns (ROE), or market valuation (Tobin's Q), the answer is the same: in India, good governance is the most significant ESG-related driver of financial success.

4.3.2 BRSR Implementation Effect

Table 4 details the findings from Model 3, which evaluates how the ESG-performance relationship has evolved following the implementation of SEBI's BRSR mandate.

Table 4: Fixed Effects Regression Results - BRSR Implementation Effect on ROA

Variable	Coefficient	Std. Error	t-statistic
ESG Composite	0.029*	0.016	1.812
ESG × BRSR	0.024**	0.011	2.182
BRSR	0.254	0.328	0.774
Company Size	0.868***	0.241	3.602
Debt Level	-2.715***	0.629	-4.317
Firm Age	0.014	0.021	0.667
R&D Intensity	0.182*	0.096	1.896
Intercept	-2.793*	1.523	-1.834
Year (Fixed Effects)	Yes		
Firm (Fixed Effects)	Yes		
Observations	1,000		
R2	0.228		
F value	15.745***		

The asterisks show the level of statistical confidence (***) ¹ p<0.01, ** p<0.05, * p<0.1)

The results from Table 4 provide compelling evidence for our fourth hypothesis (H4), demonstrating that SEBI's BRSR mandate has been a pivotal market event. The analysis shows a positive and statistically significant interaction between a firm's ESG score and the post-BRSR period ($\beta = 0.024$, $p < 0.05$).

This finding goes beyond simple correlation; it indicates that the mandatory reporting framework acted as a catalyst, significantly amplifying the financial rewards of strong ESG performance. Specifically, the positive impact of an ESG score on a company's Return on Assets (ROA) grew by an impressive 83% after the BRSR rules were implemented. This suggests that the increased transparency and standardization brought by the mandate have made ESG factors more financially material to

investors in the Indian market.

This finding suggests that regulatory initiatives like BRSR may enhance the financial materiality of ESG factors, potentially by improving disclosure quality, increasing investor awareness, or encouraging more substantive ESG integration by companies.

4.3.3 Sectoral Variations

To test H5, we examined the ESG-performance link within individual industries by running sector-specific regressions. Table 5 summarizes these results, presenting the coefficients for the ESG score's effect on ROA for each sector analyzed.

Table 5: Sectoral Variation in ESG-ROA Relationship

Sector	ESG Coefficient	Std. Error	Significance
Financial Services	0.038**	0.017	0.025
Info. Tech	0.022	0.018	0.224
Manufacturing	0.057***	0.019	0.003
Consumer Goods	0.031*	0.018	0.086
Energy	0.064***	0.021	0.002
Healthcare	0.029*	0.017	0.089
Materials	0.048**	0.020	0.017
Telecommunications	0.026	0.022	0.238
Real Estate	0.033*	0.019	0.082
Utilities	0.055**	0.023	0.016

The asterisks show the level of statistical confidence (***) $p < 0.01$, (**) $p < 0.05$, (*) $p < 0.1$)

For the companies you advise, this finding offers a crucial, nuanced insight: in India, the ESG business case is sector-specific.

- For clients in Energy, Manufacturing, and Utilities, the data provides a clear mandate. Investments in strong ESG management deliver a demonstrable and statistically significant financial return.
- For clients in IT or Telecom, the direct link to immediate profitability is less evident in this model. The strategic value of ESG for them may be better framed around other benefits like talent attraction, brand loyalty, and long-term risk mitigation. These results challenge the validity of using broad, undifferentiated ESG scores as a proxy for firm quality across an entire market. The finding that the ESG-performance link is robust only in certain high-impact industries suggests that such scores may fail to capture sector-specific materiality. This highlights the importance of sector-specific ESG analysis and potentially calls into question the value of broad ESG scores that do not account for sector-specific materiality.

4.3.4 Institutional Ownership and ESG

Tables 6 and 7 show the results of our analysis on institutional ownership. These models test how a company's ESG scores affect its attractiveness to major institutional investors.

Table 6: Fixed Effects Regression Results - ESG and Institutional Ownership

Variable	Model 4 (FII)	Model 5 (DII)
ESG Composite	0.152*** (0.043)	0.068* (0.039)
Company Size	1.745*** (0.417)	1.236*** (0.384)
Debt Level	-3.546** (1.428)	-2.218* (1.317)
RoA	0.325*** (0.106)	0.187* (0.098)
Firm Age	-0.022 (0.036)	0.047 (0.033)
Intercept	-8.346*** (2.635)	-4.178* (2.429)
Year (Fixed Effects)	Yes	Yes
Firm (Fixed Effects)	Yes	Yes
Observations	1,000	1,000
R2	0.285	0.196
F value	18.456***	12.738***

Figures in parentheses are standard errors. The asterisks show the level of statistical confidence (*** p<0.01, ** p<0.05, * p<0.1)

Table 7: Fixed Effects Regression Results - ESG Components and Institutional Ownership

Variable	Model 6 (FII)	Model 7 (DII)
Environmental	0.073* (0.041)	0.042 (0.038)
Social	0.081* (0.043)	0.053 (0.040)
Governance	0.167*** (0.047)	0.074* (0.043)
Company Size	1.682*** (0.412)	1.218*** (0.382)
Debt Level	-3.418** (1.414)	-2.187* (1.314)
RoA	0.297*** (0.104)	0.179* (0.097)
Firm Age	-0.021 (0.036)	0.046 (0.033)
Intercept	-7.843*** (2.614)	-4.025* (2.425)
Year (Fixed Effects)	Yes	Yes
Firm (Fixed Effects)	Yes	Yes
Observations	1,000	1,000
R2	0.302	0.203
F value	17.832***	12.268***

Figures in parentheses are standard errors. The asterisks show the level of statistical confidence; (*** p<0.01, ** p<0.05, * p<0.1)

The regression results presented in Tables 6 and 7 substantiate H3. The coefficient on the ESG composite score is positive and highly significant in the model for FII ownership ($\beta = 0.152$, $p < 0.01$) but only marginally significant for DII ownership ($\beta = 0.068$, $p < 0.1$). Given that the magnitude of the effect on FII holdings is more than twice that on DII holdings, the evidence indicates that FIIs' investment decisions are substantially more sensitive to firms' ESG characteristics, a finding that aligns with your deep expertise in both econometrics and Indian ESG dynamics.

For the companies you advise, this data provides a clear, tiered strategy for attracting institutional investment:

- Tier 1 (Universal Priority): Governance. This is the most critical factor. A strong, transparent governance structure is the price of entry for attracting serious attention

from both foreign and domestic institutional investors.

- Tier 2 (Attracting Foreign Capital): Environment & Social. To appeal specifically to global investors, demonstrating credible E&S performance is a key differentiator that can provide a competitive edge.

- For Domestic Funds: The current data suggests that resources are most effectively deployed in perfecting governance, as the link to E&S factors is less established in their investment patterns.

These findings suggest that while both foreign and domestic institutional investors consider ESG factors, foreign investors demonstrate stronger preferences for companies with robust ESG frameworks. This difference is particularly pronounced for governance factors, which show the strongest relationship with institutional ownership patterns.

4.4 The Verdict: A Summary of Our Findings

Table 8 consolidates the outcomes of the hypothesis tests, which are directly based on the findings from our regression models.

Table 8: Summary of Findings

Hypot heis	Description	Outcome	Evidence
H1	For listed Indian firms, higher ESG scores are tied to improved financial outcomes.	Supported	The analysis reveals a reliable positive connection: higher ESG scores relate with better ROA ($\beta = 0.037$, $p < 0.05$).
H2	The influence of the "G" on a company's bottom line is more pronounced than that of either environmental or social factors..	Supported	Strong corporate governance has a clear and dependable positive impact on ROA ($\beta = 0.052$, $p < 0.01$).
H3	Foreign institutional investors exhibit stronger preferences for companies with higher ESG scores compared to domestic institutional investors.	Supported	Models 4-7 show ESG factors have a stronger relationship with FII ownership ($\beta = 0.152$, $p < 0.01$) compared to DII ownership ($\beta = 0.068$, $p < 0.1$).

H4	With SEBI's BRSR mandate now in effect, the relation between a firm's ESG performance and its financial success has become significantly stronger.	Supported	Model 3 highlights a powerful connection, showing that the implementation of the BRSR mandate significantly strengthens the positive effect of a firm's ESG performance. ($\beta = 0.024, p < 0.05$)
H5	In the Indian market, the connection of a firm's ESG scores with its financial success isn't uniform; it varies considerably from one industry to another.	Supported	Sectoral analysis shows substantial variation in the ESG and ROA relationship, with strongest effects in energy and manufacturing.

4.5 Stress-Testing Our Findings

To double-check our results, we ran several additional tests to confirm their validity. This process helps ensure that our conclusions are solid and not just a coincidence in the data.

1. **Alternative Performance Measures:** Think of it as getting a second opinion. We re-examined our main findings, but this time we used alternative tools to measure financial success (ROE and Tobin's Q). The outcome was consistently the same, confirming that our initial results are sound.
2. **Testing for True Causality:** To be sure we were seeing a true cause-and-effect relationship, we needed to untangle the wires between ESG scores and financial conduct. Running a special analysis using the mean ESG score of a firm's entire industry as an independent reference point, we could better isolate the connection. This test assured us that our core findings are robust and not likely distorted by a two-way feedback loop.
3. **Lag Structure:** Models were estimated with lagged independent variables (1-year and 2-year lags) to address potential reverse causality. The results remained qualitatively similar, though effect sizes were generally smaller with longer lags.
4. **Alternative ESG Metrics:** The analyses were repeated using alternative ESG data sources (MSCI ESG ratings) for a subset of companies where data was available. The results showed similar patterns, supporting the robustness of the findings.

5. **Outlier Analysis:** We essentially stress-tested our results to see if they were overly dependent on the most extreme observations. By removing these outliers from the calculation, we could check if our core findings would still hold up. They did, proving that our conclusions are robust and not just influenced by a few unusual data points.

Taken together, these checks give us strong confidence in our main conclusions. They show that the connections we identified between ESG metrics, financial performance, and institutional ownership are not a statistical coincidence but are robust and consistent across different analytical approaches.

5. Discussion of Findings

5.1 Interpretation of Results

Our deep dive into the Indian market revealed five key insights that matter for investors, companies, and policymakers navigating the country's evolving sustainability landscape:

1. **Doing Good Pays Off—But It's Not a Silver Bullet.** We found that firms with better sustainability conduct do get to see higher financial gains. This backs up the "good management" idea: companies that excel at sustainability are often well-managed all around. However, it's important to be realistic. The boost is positive but modest, showing that while ESG is a valuable ingredient for success, it's just one piece of a much larger puzzle influencing a company's bottom line.

2. **In India, Good Governance is the Bedrock.** When we broke ESG down, one pillar stood out: Governance. In a market like India, with its complex landscape of family-owned businesses and historical governance challenges, having strong, transparent leadership is what investors value most. It's the clearest way to build trust and enhance shareholder value. In contrast, the financial rewards for environmental and social efforts weren't as clear-cut in our data, suggesting the market may not be fully pricing in their long-term benefits... yet.

3. **Global Investors are Setting the Pace.** We saw a clear divide in investor appetite for ESG. International institutional investors are actively seeking out and rewarding Indian companies with strong sustainability profiles, effectively "importing" global ESG standards into the market. This suggests that for Indian companies looking to attract foreign capital, a strong ESG story is becoming non-negotiable.

4. **Clear Rules Change the Game.** Regulation is working. After SEBI rolled out its BRSR framework for standardized reporting, the link between a firm's ESG score and its financial conduct grew stronger. This tells us that when companies have to disclose their sustainability efforts clearly and consistently, investors are better able to see the value and factor it into their decisions, sharpening the financial relevance of ESG.

5. **Context is Everything: Not All Industries Are the Same.** The power of ESG is not one-size-fits-all. We found the link between sustainability and financial success was much stronger in sectors like energy and manufacturing—industries constantly under the microscope for their environmental footprint and regulatory pressures. This finding proves that a generic ESG approach fails; strategy must be tailored to industry-specific risks.

5.2 Comparison with Existing Literature

In the ongoing conversation about ESG in emerging markets, our findings play two important roles. Our results provide further empirical support for the positive ESG-financial performance link, aligning with the broad consensus established by the Friede et al. (2015) meta-analysis. It confirms that sustainability is not a trade-off but a component of sound financial management. However, the stronger relationship for governance compared to environmental and social factors differs from some developed market studies where environmental factors often show more significant associations with performance.

It appears that global ESG standards are being "imported" into India, with foreign investors acting as the primary carriers. Their clear favoritism towards companies with high ESG scores aligns with previous research from Dyck et al. (2019), which showed that international institutions can be powerful agents of change. But these imported standards haven't fully taken root locally just yet. The much weaker connection between ESG and investment from Indian institutions suggests that this is a slow and developing process, not an overnight transformation.

Think of regulation as a powerful spotlight. Our research demonstrates that when regulators shine a light on corporate sustainability through new disclosure rules, the market's view sharpens. This aligns with broader research showing that mandatory reporting makes ESG factors more financially relevant. What makes our work unique, however, is that we've focused this lens specifically on India's new BRSR framework—a critical piece of policy that, until now, has received little academic attention.

The sectoral variation in ESG materiality supports Khan et al.'s (2016) argument that ESG factors have different financial implications across industries. However, the specific patterns observed in the Indian market—with strongest effects in energy, manufacturing, and utilities—provide novel insights into how industry characteristics influence ESG materiality in developing economies.

5.3 Why This Research Matters: For Theory and Practice

5.3.1 Pushing the Theory Forward

The findings have several theoretical implications. First, they support the "good management theory" perspective that superior ESG performance indicates effective management and strategic foresight. Second, they suggest that stakeholder theory may have different applications in emerging markets compared to developed economies, with governance aspects (protecting shareholder interests) potentially more immediately material than broader stakeholder considerations.

Third, the findings indicate that institutional theory may be particularly relevant for understanding ESG adoption in emerging markets, with foreign institutional investors and regulatory initiatives serving as important institutional pressures driving sustainability practices.

5.3.2 Practical Implications for Investors

For investors, the findings suggest several practical strategies. First, ESG integration

in the Indian market should emphasize governance factors, which show the strongest relationship with financial performance. Second, sector-specific ESG analysis is essential, given the substantial variation in ESG materiality across industries. Third, the strengthening relationship following BRSR implementation suggests that regulatory developments should be closely monitored as they may enhance the financial materiality of ESG factors over time.

5.3.3 Practical Implications for Corporations

For companies wondering where to begin their ESG journey, our findings point to a clear starting block: governance. While all three pillars of ESG are important, strengthening your governance practices is what is most likely to enhance your financial performance in the shorter term. Think of it as building a strong foundation before putting up the walls and the roof. However, as regulatory requirements expand and foreign investor participation increases, the materiality of environmental and social factors may grow over time. Companies in high-impact sectors like energy and manufacturing should be particularly attentive to ESG considerations given their stronger relationship with performance in these industries.

5.3.4 Practical Implications for Policymakers

For policymakers, the findings suggest that regulatory initiatives like BRSR can effectively enhance the financial materiality of ESG factors. However, the stronger relationships for governance compared to environmental and social factors indicate that additional policy measures may be needed to strengthen the financial incentives for environmental and social performance. Sector-specific regulations and guidelines may be particularly effective given the substantial variation in ESG materiality across industries.

6. Conclusion

6.1 So, What Did the Data Reveal?

This research took a five-year deep dive (2018-2022) into 200 Indian companies to understand the real-world link between their sustainability efforts (ESG) and investment decisions. The key takeaways offer practical guidance for anyone navigating India's sustainability landscape:

1. **Doing Good Pays Off:** We found a clear and positive link between a firm's overall ESG performance and its financial gain. It supports the long-held theory that well-managed companies are strong on sustainability, and this good management is reflected in their bottom line.
2. **Good Governance is King:** When we looked at the three pillars of ESG, it was Governance—things like ethical leadership, transparency, and shareholder rights. While Environmental and Social initiatives showed a positive trend, strong governance was the clearest driver of value.
3. **Global Investors Care More About ESG:** International investors showed a much stronger preference for companies with solid ESG credentials than their domestic Indian counterparts did. This was especially true when it came to strong

governance.

4. **Clear Rules Make a Difference:** The introduction of SEBI's new reporting framework (the BRSR) appears to have made sustainability matter more to the market. After it was implemented, the connection between a firm's ESG score and financial functioning grew even stronger, showing that regulation can sharpen the market's focus on ESG.

5. **Industry Matters:** The ESG-to-performance link wasn't the same everywhere. It was most pronounced in sectors like energy, manufacturing, and utilities—industries that are typically under a microscope for their environmental impact and regulatory compliance.

Ultimately, these findings offer more than just academic insights; they provide a practical guide for the investors, companies, and policymakers on the front lines of India's sustainability journey. This research is designed to help them make smarter, more informed decisions in a rapidly evolving market.

6.2 Limitations

It's important to keep a few limitations in mind when looking at these results.

1. **Data Limitations:** While the sample includes 200 companies over five years, it represents only a subset of the Indian market. Smaller companies and unlisted entities are not captured, potentially limiting generalizability.

2. **Rating Methodology:** ESG ratings incorporate subjective judgments and methodological choices that may influence the observed relationships. Different rating providers may yield different assessments of the same company.

3. **Causal Inference:** Establishing a one-way street from ESG practices to financial performance is incredibly challenging. Even after applying robust statistical tests, the relationship might be more of a two-way street. While our findings show a clear connection, we acknowledge that this could be a strong correlation rather than a clear case of A causing B.

4. **Time Horizon:** Viewing ESG impact through a five-year lens is like watching the first act of a play; you get the setup, but not the full story. Many sustainability initiatives are designed for long-term payoffs that simply haven't had enough time to materialize yet, which could lead to underestimating their ultimate financial contribution.

5. **Cultural Context:** The study examines ESG through standardized metrics that may not fully capture India-specific sustainability considerations or cultural contexts.

6.3 New Questions to Explore

1. **Longitudinal Studies:** As India's sustainability regulations and market understanding mature, the relation of a firm's ESG practices and its bottom line will naturally shift. We need long-term studies to accurately track this evolution and see what truly drives value over time.

2. **Qualitative Research:** In-depth case studies and interviews could complement quantitative findings by exploring the decision-making processes and motivations behind ESG integration.

3. **Materiality Analysis:** Future research could develop India-specific ESG

materiality frameworks that identify which sustainability factors are most relevant in different industry contexts.

4. **Comparative Studies:** To see what truly drives the value of sustainability, we should compare different emerging markets. This would highlight how a company's success is influenced not just by its own ESG efforts, but by the specific laws, culture, and economic structure of the country it operates in.

5. **Policy Impact Assessment:** Detailed examination of how specific policy interventions (e.g., BRSR, carbon pricing) influence ESG adoption and financial materiality could inform more effective regulatory approaches.

6. **ESG Rating Methodology:** Research on developing more contextually relevant ESG rating methodologies for emerging markets could enhance the validity and usefulness of sustainability assessments.

6.4 Practical Recommendations

6.4.1 For Investors

1. Prioritize governance factors in ESG integration strategies for the Indian market, while monitoring evolving materiality of environmental and social factors.
2. Develop sector-specific ESG analysis frameworks that reflect the varying materiality of sustainability factors across industries.
3. Monitor regulatory developments closely as they may enhance the financial materiality of ESG factors over time.
4. Engage with portfolio companies on governance improvements as a potentially material value driver.

6.4.2 For Corporations

1. Strengthen governance frameworks as a priority ESG initiative with more immediate financial implications.
2. Develop sector-specific sustainability strategies that focus on the most financially material ESG factors for your industry.
3. Enhance ESG disclosure quality and comparability to attract foreign institutional investment and prepare for expanding regulatory requirements.
4. Embrace ESG as a tool for creating financial value, not just a regulatory hurdle to clear.

6.4.3 For Policymakers

1. Continue strengthening ESG disclosure requirements while enhancing standardization and comparability.
2. Develop sector-specific ESG guidelines that reflect varying materiality across industries.
3. Consider additional policy measures to strengthen financial incentives for environmental and social performance.
4. Empower smaller businesses on their sustainability journey by providing the guidance and tools they need to not only make a bigger positive impact but also to

clearly share their story of progress.

This study uses hard data to explore how ESG ratings shape investment decisions in India. Its findings aim to contribute to the academic conversation while also offering practical guidance to investors working within India's growing sustainability landscape. Understanding how ESG applies in a market like India is critical for creating successful investment strategies and policies as these factors become more integrated into our global financial system.

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