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Impact of ESG Ratings on Firm Performance and Investment Decisions: Evidence from NSE-Listed Companies in India

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ABSTRACT: This study examines the impact of Environmental, Social, and Governance (ESG) ratings on firm financial performance and investment decisions among 20 companies listed on the National Stock Exchange (NSE) of India over the period 2018–2024. Utilizing a panel dataset of 139 firm-year observations spanning nine sectors, the study employs descriptive statistics, Pearson correlation analysis, Ordinary Least Squares (OLS) multiple regression, and moderation analysis. Financial performance is proxied by Return on Assets (ROA), Return on Equity (ROE), and Tobin's Q, while ESG scores are sourced from Sustainalytics and MSCI. The results confirm that ESG performance is a statistically significant positive predictor of all three financial performance metrics. The Environmental pillar is the strongest predictor of asset efficiency, the Social pillar shows the greatest influence on equity returns and market valuation, and the Governance pillar exerts a consistent, foundational effect. Revenue growth negatively moderates the ESG–ROA relationship, indicating that high-growth firms experience delayed accounting benefits from ESG investment. The findings validate Stakeholder Theory, the Resource-Based View, and Signaling Theory in the Indian corporate context and offer practical guidance for corporate managers, investors, and policymakers.

KEYWORDS: ESG ratings, firm financial performance, Tobin's Q, NSE-listed companies, sustainable finance, India

I. INTRODUCTION AND BACKGROUND

Environmental, Social, and Governance (ESG) factors have rapidly moved from voluntary corporate initiative to strategic necessity. Traditional frameworks for evaluating firm performance focused exclusively on financial indicators such as profitability, revenue growth, and shareholder returns. However, with rising global concerns over climate change, social inequality, and governance failures, the scope of evaluation has expanded to incorporate non-financial dimensions. ESG factors now serve as critical lenses through which investors, regulators, and stakeholders assess corporate sustainability and long-term value creation.

In India, ESG adoption has accelerated in response to regulatory mandates including the Companies Act 2013 (which requires eligible firms to allocate a portion of profits toward Corporate Social Responsibility activities) and the Securities and Exchange Board of India's (SEBI) Business Responsibility and Sustainability Reporting (BRSR) framework. Leading Indian corporations such as Infosys, Tata Consultancy Services, and Hindustan Unilever have integrated ESG into their core strategies and are globally recognized for sustainability performance. Concurrently, ESG rating agencies including Sustainalytics, MSCI, and Refinitiv provide standardized scores that investors use to identify resilient, well-governed, and low-risk firms.

Despite the growing significance of ESG, empirical evidence on its financial impact in India remains limited and often inconclusive. This study addresses this gap by analyzing 20 NSE-listed companies across nine sectors over a seven-year panel (2018–2024), providing robust econometric evidence on the ESG–financial performance nexus in an emerging market setting.



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II. RESEARCH PROBLEM / PROBLEM STATEMENT

The central research problem investigated in this study is the extent to which ESG ratings influence firm performance and investment decisions among NSE-listed Indian companies. Several interrelated issues motivate this inquiry.

First, inconsistency in ESG measurement persists: scores from different rating agencies (MSCI, Refinitiv, Sustainalytics) can differ substantially for the same firm due to divergent methodologies, scopes, and weighting schemes. This creates confusion among investors and limits the reliability of ESG as a standardized decision-making tool. Second, the ESG–financial performance relationship is contested in the literature, with some studies reporting positive associations, others reporting neutral or even negative results, and most focusing on developed markets. The Indian corporate landscape—characterized by unique regulatory frameworks, diverse industry structures, and varying ESG maturity—demands context-specific empirical analysis. Third, the moderating role of firm-specific factors such as revenue growth in the ESG–financial performance relationship has received insufficient attention. High-growth firms may convert ESG investments into financial value on a different timeline than mature firms, and understanding this dynamic has direct implications for corporate strategy and investor expectations.

III. OBJECTIVES OF THE STUDY

The primary objective is to analyze the impact of ESG ratings on firm performance and investment decisions for selected NSE-listed Indian companies. The specific objectives are:

- To examine the ESG disclosure performance of selected NSE-listed companies, focusing on overall ESG scores as well as individual Environmental, Social, and Governance pillar components.
- To analyze the impact of ESG determinants on financial performance measured using ROA, ROE, and Tobin's Q.
- To investigate the relationship between ESG ratings and investment decisions, particularly in terms of market valuation, investor perception, and firm attractiveness.
- To compare ESG performance across industry sectors, identifying sector-specific variations and trends in ESG adoption and its financial implications.

IV. RESEARCH QUESTIONS AND HYPOTHESES

The study tests the following primary and moderation hypotheses:

- H1: ESG performance has a significant positive impact on firm financial performance (ROA, ROE, Tobin's Q), with sub-hypotheses for individual pillars (H1a: Environmental; H1b: Social; H1c: Governance).
- H2: ESG ratings have a significant positive relationship with firm market valuation and investment attractiveness (proxied by Tobin's Q and institutional holding patterns).
- H3: Revenue growth moderates the relationship between ESG performance and financial performance (specifically ROA).
- H4–H6: Firm size, leverage, and systematic risk (Beta) significantly influence financial performance (control variable hypotheses).

V. REVIEW OF LITERATURE

The academic literature on ESG and financial performance has grown substantially, though findings remain mixed depending on geography, methodology, and rating source.

Lunawat and Lunawat (2021) examined NSE 500 and NSE 100 ESG Index firms in India using panel regression and found that ESG index-listed firms demonstrate better operational and financial performance, with governance scores significantly impacting financial outcomes—providing the closest Indian-market precedent for the present study.

Ahmad, Al-Faryan, and Al-Qahtani (2023) used panel data models with fixed and random effects across multiple markets and found a significant positive effect of ESG performance on ROA, ROE, and Tobin's Q, with governance effects being the strongest among the three pillars.



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Ameer and Zainuddin (2023) examined 36 countries using fixed-effects panel regression and found that ESG disclosure has a significant positive effect on firm performance, particularly on market-based measures—establishing a strong cross-country benchmark.

Tabur (2022) demonstrated that the direction of the ESG–ROA relationship depends on which rating agency's scores are used: Refinitiv scores correlated negatively with ROA while Bloomberg scores showed a positive correlation, highlighting that rater choice is not methodologically neutral.

Malik and Kashiramka (2023) analyzed 272 NSE-listed Indian firms and found that ESG disclosure is positively associated with financial performance and market valuation, though industry characteristics introduce variation—underscoring the importance of sector controls in Indian ESG research.

Shukla, Ramanathan, and Patnaik (2025) documented significant ESG rating disagreements in Indian markets, calling for standardized methodologies tailored to Indian regulatory requirements—a gap this study acknowledges through its dual-agency data sourcing.

The identified research gap this study addresses is the limited panel evidence on ESG–performance dynamics specifically for NSE-listed firms using recent data (2018–2024), combined with an underexplored moderation analysis involving revenue growth as a firm-level contextual variable.

VI. PROPOSED METHODOLOGY

6.1 Research Design

The study adopts a quantitative and explanatory research design combining cross-sectional and time-series data (panel data) for 20 purposively selected NSE-listed companies over 2018–2024 (N = 139 firm-year observations). A deductive approach is followed: hypotheses derived from theory and prior literature are tested using empirical secondary data.

6.2 Sample Selection

Twenty companies were selected based on availability of ESG data from Sustainalytics or MSCI, large/mid-cap market capitalization, multi-sector representation (IT, Consumer Goods, Healthcare, Banking & Finance, Industrials, Utilities, Consumer Discretionary, Energy, Materials), and consistency of financial reporting over the study period. This purposive sampling ensures reliable, comparable data across the panel.

6.3 Data Sources

All data is secondary and publicly available:

- ESG Scores: Sustainalytics (12 firms) and MSCI (8 firms)
- Financial Performance Data (ROA, ROE, Tobin's Q): Company annual reports, NSE filings, CMIE Prowess
- Market Data (Beta, stock prices, institutional holdings): NSE India, Bloomberg

6.4 Variables

Independent Variables: Overall ESG Score, Environmental (E) Score, Social (S) Score, Governance (G) Score (all scored 0–100).

Dependent Variables: ROA (Net Income / Total Assets × 100), ROE (Net Income / Shareholders' Equity × 100), Tobin's Q (Market Value / Book Value of Assets).

Moderating Variable: Revenue Growth (annual % change in revenue).

Control Variables: Firm Size (ln of total assets), Debt-to-Equity Ratio, Beta (systematic risk).

6.5 Econometric Models

Base OLS Model: $Y_{it} = \beta_0 + \beta_1 \cdot \text{ESG}_{it} + \beta_2 \cdot \text{FirmSize}_{it} + \beta_3 \cdot \text{DE_Ratio}_{it} + \beta_4 \cdot \text{RevGrowth}_{it} + \beta_5 \cdot \text{Beta}_{it} + \varepsilon_{it}$ (estimated separately for ROA, ROE, and Tobin's Q)

Moderation Model: $\text{ROA}_{it} = \beta_0 + \beta_1 \cdot \text{ESG_c} + \beta_2 \cdot \text{RG_c} + \beta_3 \cdot (\text{ESG_c} \times \text{RG_c}) + \beta_4 \cdot \text{Controls} + \varepsilon_{it}$

ESG and Revenue Growth variables are mean-centered prior to interaction term computation to minimize multicollinearity. Analysis is conducted using Python (pandas, numpy, statsmodels, matplotlib).



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VII. KEY FINDINGS

7.1 ESG Performance Has Improved Significantly Over Time

Average ESG scores rose from 50.94 in 2018 to 60.49 in 2024—a cumulative gain of 18.7%. The Social pillar showed the most sustained growth (52.95 to 62.17), while the Governance pillar accelerated post-2021, aligned with SEBI's heightened scrutiny of board independence. Concurrently, average ROA improved from 9.09% to 11.28% and average ROE from 18.78% to 24.54%, indicating a positive co-movement between ESG commitment and financial profitability.

7.2 ESG Significantly Enhances Financial Performance (H1 Supported)

The OLS regression models explain 78.09% of ROA variance, 59.90% of ROE variance, and 55.54% of Tobin's Q variance. ESG Score is a positive and highly significant predictor of ROA ($\beta = 0.295$, $p < 0.001$), ROE ($\beta = 0.894$, $p < 0.001$), and Tobin's Q ($\beta = 0.217$, $p < 0.001$), firmly supporting H1.

7.3 ESG Pillar Analysis (H1a, H1b, H1c All Supported)

The Environmental Score is the strongest predictor of ROA ($\beta = 0.421$, $p < 0.001$), reflecting how energy management and waste reduction improve asset efficiency. The Social Score is the dominant predictor of ROE ($\beta = 0.912$, $p < 0.001$) and Tobin's Q ($\beta = 0.218$, $p < 0.001$), suggesting that human capital and stakeholder engagement generate the greatest equity value. The Governance Score is consistently significant across all three models, confirming its foundational role.

Table 1: Summary of Hypothesis Testing Outcomes

H#	Hypothesis	Test Statistic	Result	Verdict
H1	ESG → ROA, ROE, Tobin's Q	$\beta=0.295$, $p<0.001$	Supported	✓ SUPPORTED
H1a	Environmental Score → Financial Performance	$\beta=0.421$, $p<0.001$	Supported	✓ SUPPORTED
H1b	Social Score → Financial Performance	$\beta=0.912$, $p<0.001$	Supported	✓ SUPPORTED
H1c	Governance Score → Financial Performance	$\beta=0.218$, $p<0.01$	Supported	✓ SUPPORTED
H2	ESG → Market Valuation (Tobin's Q)	$\beta=0.217$, $p<0.001$	Supported	✓ SUPPORTED
H3	Revenue Growth moderates ESG–ROA	$\beta=-0.772$, $p<0.05$	Partial (–ve)	~ PARTIAL
H4	Firm Size impacts performance	$\beta=-6.365$, $p<0.001$	Supported (–ve)	✓ SUPPORTED
H5	Leverage impacts performance	$\beta=-0.581$, $p<0.001$	Supported (–ve)	✓ SUPPORTED
H6	Beta (risk) influences performance	$\beta=-6.314$, $p<0.05$	Supported (–ve)	✓ SUPPORTED

7.4 ESG Enhances Market Valuation and Investment Attractiveness (H2 Supported)

Top ESG-performing firms—Infosys (ESG 65.42), Hindustan Unilever (64.49), and TCS (61.97)—recorded the highest Tobin's Q values (6.78, 12.99, and 12.75 respectively), demonstrating that capital markets assign significant valuation premiums to ESG excellence. A positive correlation between ESG Score and institutional holding patterns ($r = 0.43$, significant) further confirms that ESG-oriented firms attract sophisticated institutional investors.



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7.5 Revenue Growth Negatively Moderates ESG–ROA (H3 Partially Supported)

The interaction term (ESG \times Revenue Growth) is statistically significant ($\beta = -0.772$, $p < 0.05$) but negative, contrary to the directional prediction of H3. High-growth firms reinvest aggressively in expansion and capital expenditure, diverting resources away from translating ESG investments into immediate accounting profitability. The direct positive ESG effect on ROA remains robust ($\beta = 1.666$, $p < 0.001$), indicating that growth delays rather than eliminates ESG's financial benefits.

7.6 Sector-Wise Heterogeneity

IT (ESG 61.58) and Consumer Goods (60.75) sectors lead in both ESG scores and financial performance, supporting the ESG–performance hypothesis in asset-light, brand-sensitive industries. The Utilities sector leads on Environmental scores (61.87) yet records the lowest Tobin's Q (1.58), illustrating that capital-intensive, regulated industries face structural barriers to converting environmental leadership into market valuation premiums. Materials and Energy sectors, with the lowest ESG scores, also record the weakest financial performance.

VIII. EXPECTED CONTRIBUTION AND SIGNIFICANCE

8.1 Theoretical Contribution

This study makes four primary theoretical contributions to the ESG and sustainable finance literature. First, it provides robust panel evidence validating Stakeholder Theory in an emerging market context: firms that actively manage stakeholder relationships through ESG practices—particularly the Social pillar generate superior equity returns and market valuation premiums. Second, the Resource-Based View (RBV) is corroborated: ESG practices function as strategic, non-replicable resources (energy efficiency, talent management, governance quality) that generate sustainable competitive advantage reflected in higher ROA and Tobin's Q. Third, Signaling Theory is validated through the strong ESG–Tobin's Q relationship: ESG scores function as credible signals of managerial quality and long-term value orientation, reducing information asymmetry and attracting institutional investors. Fourth, the negative moderation finding extends Agency Theory, identifying a temporal agency dilemma in high-growth firms where ESG investments generate deferred rather than immediate accounting returns.

8.2 Practical Contribution

For corporate managers, the study quantifies ESG's financial return: a one-unit increase in ESG Score is associated with a 0.295 percentage point increase in ROA and a 0.894 percentage point increase in ROE, enabling firms to treat ESG investment as a quantifiable value driver rather than a compliance cost. The pillar-wise hierarchy—Social dominates equity returns, Environmental drives asset efficiency, Governance provides a foundational foundation—offers strategic clarity for ESG investment allocation.

For institutional investors and fund managers, the positive ESG–Tobin's Q relationship ($\beta = 0.217$, $p < 0.001$) provides empirical validation for integrating ESG scores into equity valuation models. The absence of a significant ESG–stock return relationship cautions against expecting immediate excess returns and supports a long-term, value-oriented investment thesis.

For policymakers and SEBI, the evidence that ESG adoption grew substantially from 2018 to 2024 validates the regulatory approach. However, significant inter-sector variation in ESG scores suggests that sector-specific ESG guidelines and standardized, mandatory rating methodologies would accelerate laggard sectors and enhance the reliability of ESG as an investment decision tool.

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