

# Recent Developments in Research on the Impact of ESG on Corporate Value

Qichen Zhang \*

Department of Overseas Chinese Academy, Capital University of Economics and Business  
University, Beijing, China

\* Corresponding author: 32022140139@cueb.edu.cn

**Abstract.** ESG (Environmental, Social, and Governance) has become an increasingly prominent topic in the investment field. Questions such as whether ESG can create value for companies, the credibility of ESG investments, and whether ESG should be incorporated into my long-term investment plan are crucial considerations. Many scholars have conducted research from various perspectives to address these questions. This article summarizes relevant literature and answers the impact of ESG on corporate value and the factors influencing ESG's impact on corporate value. The research findings are as follows: 1. ESG has a generally positive impact on corporate value, with some factors showing inhibitory effects or no significant correlation. 2. ESG primarily affects corporate value through aspects such as market valuation, financing costs, innovation capability, and reputation. 3. The impact of ESG on corporate value varies depending on the ownership structure and industry of the company. Based on these findings, companies should decide whether to enhance their ESG performance based on various factors such as their operational situation, industry composition, and ownership structure.

**Keywords:** ESG Performance, Corporate Value.

## 1. Introduction

The impact of ESG (Environmental, Social, and Governance) on corporate value has become a focal point in the financial industry. With the introduction of initiatives like the Principles for Responsible Investment (PRI) and the emergence of ESG rating agencies, a company's ESG score has become a crucial factor in ESG investment strategies. Companies with high ESG scores can have their stocks included in ESG funds, leading to greater ecological and social benefits. However, there are differences of opinion between companies and investors regarding ESG investments, with investors being uncertain and not fully recognizing the long-term value of ESG.

According to a report by PwC titled "Mind the gap: the continued divide between investors and corporates on ESG," only 27% of investors fully incorporate ESG into their long-term investments. Achieving a high ESG rating may also require significant investment from companies, which can be challenging to justify. Hence, there is considerable debate about the impact of ESG on corporate value.

As scholars delve deeper into research on the relationship between ESG and corporate value, the focus has shifted from simply assessing whether ESG has a positive or negative impact to understanding the mechanisms through which ESG affects corporate value. Based on existing research, it is evident that ESG performance significantly influences a company's book value and market value. ESG performance achieves value effects through different channels [1]. This suggests that ESG impacts corporate value through two dimensions, raising new questions about the mechanisms by which ESG affects corporate value in these two dimensions.

For instance, research has explored how ESG performance influences a company's market [2] and the impact of ESG ratings on corporate innovation [3,4]. Many studies have investigated the mechanisms through which ESG affects corporate value. This article aims to integrate these existing studies and provide insights into the mechanisms through which ESG influences corp

## **2. The Effect of ESG on Firm Value**

### **2.1. Positive Effects**

Most scholars believe that ESG advantages can enhance corporate value [5]. In addition to the overall impact of ESG on corporate value mentioned earlier, research also examines the effects of different ESG factors on corporate value. For example, ESG disclosure can improve corporate financial performance [6], with studies focusing on the impact of ESG disclosure on corporate value. ESG controversies can have significant positive effects on a company's market value [7], and when a company's ESG rating improves, its corporate value also increases [8]. The mentioned studies investigate the impact of factors such as ESG disclosure, ESG controversies, and ESG ratings on corporate value. It is evident that both the overall ESG performance and individual ESG factors can have a positive impact on corporate value.

### **2.2. Inhibitory Effects:**

Some research also suggests that ESG can have inhibitory effects on corporate value. For instance, increased ESG scrutiny can decrease corporate value [7], indicating negative impacts on corporate value due to other ESG factors. Additionally, when isolated, ESG disclosure can also reduce corporate value [7]. This is another example of a factor that has a positive impact on corporate value but can have inhibitory effects under specific conditions when isolated. Companies in ESG-sensitive industries may experience negative impacts on their value [9], indicating inhibitory effects on specific types of companies.

## **3. Factors of ESG Affecting Enterprise Value**

Based on the research reports of existing scholars, ESG performance has a significant positive impact on both a company's book value and market value [1]. Therefore, the following sections will separately summarize the mechanisms through which ESG affects corporate value in terms of its impact on book value and market value, as well as how ESG performance achieves value effects through different channels.

### **3.1. Book Value and Market Value:**

Many factors influence a company's book value and market value, including but not limited to the following: Improved ESG performance by publicly traded companies can increase the company's market capitalization, with the company's financial performance serving as a significant mediator in this relationship. Operational capabilities play an essential intermediary role in how ESG performance affects a company's market value [10]. Investors exhibit a preference for ESG investments and may not overly focus on a target company's current operational performance, leading to increased investor interest in companies with strong ESG performance [2]. Enhancing ESG performance can help companies reduce financing costs, improve innovation capabilities, and profitability [11,12]. ESG performance enhances earnings value relevance through mechanisms such as capability transformation, information transmission, and corporate reputation [1,13].

### **3.2. Different Channels for Achieving Value Effects**

The mechanisms through which ESG performance achieves value effects revolve around two extensively researched aspects: reputation and innovation.

**Innovation:** Scholars generally agree that a company's ESG performance can promote green innovation [3]. Higher levels of ESG practices enhance a company's ability to access social capital, improve management's farsightedness, alleviate financing constraints, and thereby stimulate innovation [8,14]. ESG ratings significantly promote both the quantity and quality of green innovation in companies, acting as an intermediary by easing financial constraints and increasing managers' environmental awareness [4].

Reputation: Researchers believe that ESG performance and its three dimensions have a significant promotional effect on a company's reputation [15]. Reputation and ESG performance are often linked in studies, with improved ESG performance leading to an enhancement in reputation [13]. Current research suggests that a company's strong ESG performance can enhance innovation performance through reputation effects and resource effects [16]. Unlike innovation, which directly impacts a company's value, reputation acts as an intermediary in the relationship between ESG performance and green innovation [3], playing a crucial role in indirectly influencing innovation.

These findings demonstrate that ESG performance affects corporate value not only through its direct impact on financial metrics but also through its influence on reputation and innovation, which can have significant, albeit indirect, effects on a company's value.

#### **4. The difference analysis of ESG influence on enterprise value**

In analyzing each academic study, it was found that many scholars often mention two major sources of heterogeneity in the "Differential Analysis" section: state-owned enterprises vs. privately-owned enterprises and variations across different industries. ESG exhibits varying impacts on the corporate value of these different types of companies. This phenomenon is closely related to the effects and factors influencing ESG's impact on corporate value, and it also reflects the significance of ESG in influencing corporate value. Therefore, the following sections will consolidate the research findings from different academic reports regarding this phenomenon [17].

##### **4.1. Differences between State-Owned and Non-State-Owned Enterprises:**

Heterogeneity analysis of ESG primarily centers around differences in corporate ownership, and there have been many studies in China on the distinctions between state-owned and non-state-owned enterprises. Most scholars believe that for state-owned enterprises, ESG performance has a more pronounced positive impact on the value of non-state-owned enterprises [8]. It is widely recognized that ESG's value-creating function diminishes the differences in operational objectives between state-owned and non-state-owned listed companies. Furthermore, institutional investors' preference for ESG is more prominent in non-state-owned listed companies [2]. Not only does heterogeneity exist in the overall impact of ESG on company value, but there are also variations in the factors through which ESG influences the value of different companies. For example, regarding the impact of ESG on company reputation, ESG performance in non-state-owned enterprises has a more significant effect on enhancing innovation performance when compared to state-owned enterprises [1,16].

Scholars suggest that the reasons behind this heterogeneity may be that state-owned enterprises, due to their natural connection with the government, are more likely to receive government funding and financial institution loans, resulting in weaker external

##### **4.2. Heterogeneity Across Different Industries**

ESG exhibits significant heterogeneity in its impact on the corporate value of companies in different industries. One common observation is that ESG performance has a more pronounced positive effect on increasing corporate value for heavily polluting companies compared to lightly polluting ones [18]. Similarly, in the context of different industries, companies in the high-tech sector tend to benefit more from ESG performance in terms of enhancing corporate value compared to companies in traditional industries [8].

There are two main reasons behind this phenomenon. First, pollution-intensive companies are often more attentive to their environmental practices, leading to improved environmental performance. This, in turn, helps reduce environmental risks and regulatory costs, which is recognized and appreciated by investors, contributing to improved ESG performance [18]. Second, companies in heavily polluting industries often face more significant financing constraints compared to those in less polluting industries [8]. The heightened financing constraints in these sectors reflect a preference for safety in investments, which institutional investors tend to prioritize. This analysis demonstrates

that ESG's impact on corporate value can vary significantly depending on the industry in which a company operates. Specifically, it has a more pronounced positive effect on companies in industries associated with environmental concerns, such as pollution-intensive sectors, as well as companies in high-tech industries where innovation and sustainability are often highly valued.

## 5. Conclusion

This article summarizes recent academic research on the impact of ESG on corporate value and provides insights into the effects, mechanisms, and variations across different ownership structures and industries. The key findings can be summarized as follows:

ESG generally has a positive impact on corporate value, primarily because several ESG factors have a positive influence on company value. However, there are exceptions where specific factors, under certain conditions or within certain industries, may have a restraining effect on corporate value. ESG performance primarily influences corporate value through factors such as market capitalization, investor preferences, financing costs, innovation capabilities, and reputation. These factors collectively contribute to the overall impact of ESG on corporate value. The impact of ESG on corporate value varies across different ownership structures and industries. Non-state-owned or smaller enterprises tend to experience more significant improvements in corporate value due to ESG performance. In addition, industries such as high-tech and heavily polluting sectors are more influenced by enhanced ESG performance.

Based on the research findings, several implications can be drawn:

First, companies aiming to improve their ESG performance should conduct industry-specific and internal assessments as ESG impacts can vary depending on specific factors and industry conditions. Even though ESG generally has a positive influence on corporate value, companies should be prepared for potential challenges. Second, smaller enterprises should pay particular attention to ESG performance as it can significantly affect their reputation and gain them advantages in investor preferences. ESG can offer a competitive edge in areas such as environmental responsibility and digitalization.

In conclusion, this article provides valuable insights into the complex relationship between ESG and corporate value. It underscores the importance of considering industry-specific factors and highlights the potent.

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