

Research on the Impact of ESG Investment on Corporate Financial Performance

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Abstract. This study examines the impact of ESG investment on corporate financial performance across different industries. It explores the relationship between the stakeholder theory, sustainable development theory and ESG, revealing that long-term ESG resource allocation—distinct from discretionary CSR—needs supply-chain coordination and attention to economic, environmental and social sustainability. This research shows a positive cyclical relationship between ESG performance and financial indicators (ROA, ROE), with financial flexibility aiding ESG investment realization. The research indicates that ESG investment enhances positive role in enhancing the profitability and operational capabilities, but has limited impact on debt repayment risk mitigation. To achieve ESG investment, it is necessary to formulate the correct strategic policies and ensure that factors such as technology, funds, laws, and human resources are all in place and meet the requirements. Finally, the article specifically outlines the advantages and disadvantages of ESG investment, helping enterprises make a judgment on whether they need to engage in ESG investment based on their own circumstances. This paper, based on previous theoretical analysis and empirical studies, provides new support for ESG investment to become a criterion for managers' investment decisions and a means of management innovation.

Keywords: ESG investment; financial performance; sustainable development; financial flexibility; management innovation.

1. Introduction

With the advancement of technology and the development of civilization, environmental, social and governance (ESG) investments have increasingly become key factors in corporate strategies and investor decisions. Companies in various industries around the world are gradually paying attention to sustainable development, including but not limited to economic, environmental and social aspects. The financial industry places even greater emphasis on the sustainable development of investment. Under the impact of global warming and the outbreak of the pandemic, social responsibility and environmental protection have become the focus of public attention. Stakeholders not only demand that enterprises ensure economic sustainability, but also require them to actively assume social responsibilities. The supervisory authorities in various regions, such as the EU's "Sustainable Finance Disclosure Regulation" (SFDR) and the US Securities and Exchange Commission (SEC), require enterprises to enhance the disclosure of ESG in their annual financial statements. This further proves that ESG has become an important indicator for evaluating whether a company is worthy of investment and for assessing its social standing.

ESG investments have shown stronger resilience during economic uncertainty [1]. The researchers analyzed the changes in global financial markets during the COVID-19 pandemic and the Russia-Ukraine conflict based on data from October 2021 to February 2024. The research results have emphasized the crucial basis for judging the importance of incorporating ESG factors into long-term investments.

Many industries have also joined the ESG development process, such as the renewable energy industry. Tesla voluntarily disclosed the sources of raw materials in its supply chain, facilitating traceability. In terms of social aspects, Tesla places great emphasis on maintaining a balanced gender ratio within the organization, reducing issues of racial discrimination and the imbalance in the ratio of men to women. Tesla releases impact reports every year, ensuring its business is transparent and actively accepting social supervision.

This article not only focuses on exploring the short-term impact of ESG investment on the financial performance of enterprises, but also incorporates the long-term impact into the research scope. Specifically, the study will: Quantify the short-term impact of ESG investment on financial performance, such as changes in return on equity (ROE) within 1-2 years. Examine the long-term impact of ESG investment on the value of enterprises, including brand value and customer loyalty. Understand how financial enterprises can utilize ESG to enhance their operations and overall value. Furthermore, the research will delve into the relationship between ESG investment and corporate financial performance by: Assessing the extent to which ESG investment contributes to return on equity (ROE) and return on assets (ROA). Examining whether there are significant differences in ESG investment among different industries and enterprises of different sizes.

This comprehensive approach will provide a detailed understanding of the role of ESG investment in corporate financial performance and strategic decision-making.

This study aims to deeply explore the relationship between ESG investment and corporate financial performance. Specifically, it addresses the extent to which ESG investment contributes to return on equity (ROE) and return on asset (ROA). Moreover, the research also examines whether there are significant differences in ESG investment among different industries and enterprises of different sizes.

2. Research on the Impact of ESG Investment on Corporate Financial Performance

2.1. The Definition of ESG Investment and a brief Description of its Development History

2.1.1 The definition of ESG investment

ESG integrates the three factors of environment, social, and governance [2]. Throughout this paper, ESG investment is confined to companies' own allocation of resources toward environmental, social and governance initiatives aimed at improving long-term financial performance, rather than to asset-managers' portfolio selection criteria.

2.1.2 Description of its development history

Since 1970, ESG has been increasingly valued by more and more enterprises. In 1997, the Global Reporting Initiative (GRI) was established, aiming to establish an accountability framework for enterprises. In 2004, GRI first proposed and implemented ESG. Nowadays, more and more enterprises, investors and governments have begun to widely apply the ESG theory. Although there is no unified standard, companies that score higher on ESG aspects attract more investors. This not only indicates that the enterprise has a proactive operation approach and strong profitability, but also shows that the enterprise can undertake more social responsibilities, gain the trust of stakeholders, and be more attractive to investors who pursue green investment. Just as Wang and Phillips-Fein have pointed out, "Far from being a new phenomenon, ESG is a modern form of corporate citizenship tailored to the shifting public expectations of business" [3].

2.1.3 The relationship between stakeholder theory and ESG

The theory of stakeholders provides strong support for the rationality of ESG. Stakeholder theory (ST) is a theory of business ethics and organizational management [4]. The success of an enterprise is not only determined by its own operational strategy, but also depends on the support from various stakeholders, including shareholders, employees, customers, and every part of the supply chain. Therefore, ESG investment has become a strategic approach that enables enterprises to align their operations with the expectations of stakeholders. If an enterprise wants to enhance its brand awareness, increase the loyalty and satisfaction of customers and employees, reduce the employee turnover rate and customer churn rate, it can achieve this by improving the working environment, enhancing employee benefits, and ensuring the transparency of enterprise operations, thereby having a positive impact on the financial situation and operational performance. In terms of brand loyalty, the most typical example is Apple Inc. The evaluated products have a high rate of repeat purchases, and

customers pay a high price to purchase iPhones due to the brand effect of Apple. Apple's sales and profit margins have been steadily increasing over the years, resulting in an ROE of 50%, which is significantly higher than the average level of its peers. While Apple's above-peer ROE coincides with high customer loyalty, further evidence is required to isolate the marginal contribution of ESG-specific actions from broader brand and technology effects. As a core stakeholder, consumers' behavioural preferences are significantly positively correlated with a company's financial performance, and customer loyalty is a predictor of a company's long-term financial resilience. Apple's above-peer ROE coincides with its high customer-retention rates; while this alignment supports stakeholder theory, further evidence is required to establish the extent to which ESG-specific actions, rather than broader brand strategies, drive the observed financial outcome.

2.1.4 The relationship between sustainable development theory and ESG

The theory of sustainable development holds that in order to achieve long-term goals of the enterprise, attract more reliable investments, enhance the enterprise's reputation and social status, it is necessary to incorporate the protection of the social environment and the improvement of social welfare into the core of the enterprise's operations. And ESG investment perfectly aligns with the theory of sustainable development. To effectively contribute to the grand challenge of sustainable development, a clear and transparent communication about ESG conduct is essential to retain investors and stakeholders' trust [5]. Through ESG investment, enterprises place greater emphasis on environmental protection and improving people's livelihood. For instance, in the upstream and downstream industrial chains, efforts should be made to reduce waste of raw materials and emissions of pollutants, improve the working environment for employees, and ensure the social insurance for stakeholders. These methods effectively reduce social and social risks, ultimately achieving the goal of enhancing the long-term competitiveness of the enterprise.

2.2. The Definition and Measurement Standards of Enterprise Financial Performance

2.2.1 Definition of financial performance

“Corporate financial performance is an overview of the company's financial status report over a period of time to access how successful and profitable a company is in producing revenue” [6]. The performance of the operator in the company's operation is mainly measured by evaluating the contributions and results achieved in the management, growth and development of the enterprise. These evaluation indicators include but are not limited to asset turnover ratio, profit margin ratio, current ratio, ROA, ROE, etc. Theoretically, ESG investment has a positive impact on a company's long-term performance through market value channels such as brand, reputation, and customer loyalty. However, these non-financial indicators are difficult to quantify, so this article lists accounting indicators such as ROE and ROA to measure the short-term financial performance. These two accounting indicators demonstrate the operability of the data and correspond to the research questions presented in the introduction. Financial performance measures an enterprise's ability to create value for assets and to sustain its operations. Furthermore, financial performance is closely related to investors' decisions. Only when a company achieves positive financial performance will investors consider investing more funds to ensure the sustainable operation of the enterprise.

2.2.2 Measurement standards and commonly used financial performance indicators

Before delving into the discussion of business performance, it must first address an issue that cannot be ignored: on what measurement standards should be judged whether business performance is positive or negative?

Based on accounting and disclosure standards, a standard for measuring an enterprise's financial performance has been established. From an international perspective, the International Financial Reporting Standards (IFRS) provide a unified framework for global accounting basis. Under IFRS, financial statements are prepared under an accrual accounting system, with the focus on recognizing revenue, matching expenses with revenues, and reflecting the profitability and resource utilization of the enterprise. American enterprises actively disclose financial data in their annual financial

statements, which can be used to calculate performance indicators such as ROA and ROE. For example, ROE measures the ability of a company to generate returns on the capital invested by shareholders. ROA measures the ability of an enterprise to utilize its assets. EPS measures the earnings per share and the value of shareholders. The current ratio tests a company's ability to repay short-term debts.

2.2.3 The specific measurement methods of financial performance indicators

In ESG investment, these financial performance indicators are also referred to as dependent variables. Through the analysis of samples from various industries, it can be seen that the specific measurement indicators of ESG investment are closely related to financial indicators (ROA, ROE). For instance, in the study conducted by Ibishova, Misund, and Tveterås, the main focus was on examining the relationship between carbon emissions and corporate performance [7]. Drawing on 2,768 firm-level observations, the study shows that within high-carbon sectors, an immediate rise in emissions may deliver a brief revenue uptick; however, when such intensity persists, ROE subsequently declines, underscoring the urgent need for emission cuts. In carbon-heavy industries—autos, new energy and manufacturing—gradual abatement not only reshapes capital structure but also lifts energy efficiency, ultimately improving asset returns.

2.3. Analysis of the Specific Impact of ESG Investment on Corporate Financial Performance

2.3.1 Investment in innovation affects a company's profitability

ESG investment can significantly enhance the profitability of enterprises. Companies with high ESG indicators usually have a high social status, numerous stakeholders, and characteristics such as brand loyalty and low employee turnover rates. Jalu et al. employed a structural development model, and consumers' perception of green value has an indirect impact on green brand loyalty and a direct impact on green brand innovation [8]. The higher the loyalty of the enterprise, the higher the product sales rate will be, thereby enhancing the profitability. As a result, the return on assets, return on equity, and profit margin are generally higher than those of companies that do not engage in ESG investments. Yakdehige, J made analysis which reveal that there is always a positive correlation between ESGP and FFP [9].

Through ESG, especially the social aspect of it, enterprises implement dynamic measures for energy conservation and emission reduction, which causes a turning point in ROE. It shifts from a negative correlation to a positive one. According to the research conducted by Shahrour, Arouri and Lemand, investing in sustainable development projects can lead to an increase in costs and a decline in profitability in a short period of time [10]. However, when the research and development expenses are directly used for innovation and technological investment, it may significantly enhance the company's ability to reduce carbon emissions, thereby improving overall performance and having a positive impact on ROA and ROE.

ESG investment requires enterprises to manage comprehensively throughout the upstream and downstream of the industrial chain, and to innovate in areas such as product development and operation, then enhancing the long-term competitiveness of the enterprises. Environmental innovation as one of the vital investment approaches [11]. Enterprises can achieve this by implementing sustainable development practices. They can transform their supply chain and service chain into environmentally-friendly processes related to eco-friendly products, thereby reducing energy consumption and the exploitation of natural resources. Through these sustainable practices, enterprises can build a green brand to gain market trust, obtain high pricing opportunities, and occupy a higher market share among consumers with a strong environmental awareness. Therefore, innovations related to ESG investment can help enterprises stand out in the market, enhance their long-term profitability and improve their financial performance.

Establishing a green brand image will enhance the brand's premium value and improve financial performance. One of the most typical examples is Ben&Jerry's. Before engaging in ESG investment,

Ben&Jerry's had already become an independent green brand. The green strategy and positioning have enabled Ben&Jerry's to cultivate a group of loyal customers and achieve higher performance.

2.3.2 The risk mitigation effect of ESG investment on corporate debt repayment ability is not significant

Solvency reflects a company's ability to meet its long-term debts. However, as the market continues to expand and become more complex, the ability to repay debts is also closely linked to ESG. Recent studies have shown that companies that actively engage in ESG investment usually have higher credibility, which enhances their borrowing capacity, reduces borrowing costs, enables them to have more funds to increase market share, and thereby improves their solvency. It is found that the company's current ESG performance is positively correlated with its current solvency, and there is no lag; between solvency and ESG performance in high-pollution enterprises is stronger than that of non-high-pollution enterprises [12]. If the ESG performance is poor, one will face issues such as legal fines, a decline in social status, damage to reputation, and even the inability to repay debts on time.

However, the company's financing capabilities also have an adverse effect on ESG investments. Li conducted a study using companies listed on the Hong Kong Stock Exchange as samples, and proved that ESG performance is correlated with the financial flexibility of state-owned enterprises [13]. Therefore, a company with strong financing capabilities has more funds to invest in ESG, resulting in better ESG performance and promoting the improvement of its financing capabilities. Although better ESG scores are generally linked to lower borrowing costs, this relationship is contingent on existing leverage: highly leveraged SOEs may face short-term cash-flow pressure when ramping up ESG expenditure, suggesting that the net impact on solvency is conditional on financial slack.

2.3.3 The impact of ESG investment on a company's operational capabilities

The operational capability of a company refers to the ability of the company to generate profits by managing and operating its assets and assessing the efficiency of such operations. It can help managers understand the profits and problems of the enterprise, and make more decisive decisions. ESG investment can have a positive impact on an enterprise's operational capabilities through accurate risk management, enhancing employee loyalty and innovation capabilities, and increasing the utilization rate of assets. The most notable example is the hotel management industry. Chung, Nguyen, and Nguyen found that ESG can indeed enhance hotels' efficiency [14]. The study employed a sampling survey method to investigate 24 international hotels that were in operation from 2013 to 2019. Using the DEA method and regression analysis, it was concluded that for every 1-point increase in ESG score, the hotel's capital turnover rate would increase by 0.0035, and the loss per room would decrease by 4.8%; in the hotel segment examined, each ESG-score increment corresponds to a modest turnover gain, and generalising this magnitude to other sectors warrants caution. Social conditions and environmental circumstances play a crucial role in enhancing the operational efficiency of hotel enterprises. By conducting ESG investments, enterprises can effectively enhance operational efficiency before and after a crisis, helping them better mitigate losses and resume and rebuild their business operations.

3. Feasibility and Strategy Analysis of ESG Investment

3.1. Clarify the Specific Implementation Steps of the ESG Strategy Policy

Roughly 90% of studies find a nonnegative ESG–CFP relation [15]. For instance, Starbucks' initiative of encouraging customers to bring their own cups to reduce the use of disposable cups not only embodies its green strategy but also gains the appreciation and trust of customers, thereby outperforming other brands in terms of profitability. Therefore, implementing ESG investment holds a central position in the corporate operation philosophy, and it is particularly important to correctly implement ESG policies.

3.1.1 Formulate ESG strategic policies and goals

To implement a successful ESG investment strategy, the first step is to formulate clear and operational policies and goals. This requires enterprises to link their core values with the purpose of ESG investments and integrate them with the company's long-term goals. This process must ensure compliance with laws and regulations, be in line with the enterprise's own development strategy, and fully take into account the expectations of stakeholders. For instance, in terms of the environment, "reducing carbon emissions" needs to be achievable and measurable.

3.1.2 Establish an ESG investment management system

After establishing an operational ESG investment strategy and setting expected goals, enterprises need to establish an ESG investment management system to coordinate planning and ensure that all employees of the company are moving forward towards a unified strategic goal. The organization needs to start from aspects such as detection indicators, technical platforms, and process systems, and build a complete governance system.

3.2. Feasibility Analysis of ESG Investment

Implementing ESG investment requires continuous and stable financial support, technical support, legal and regulatory support, as well as human resource support. This article takes Unilever as an example and conducts a detailed analysis from these four aspects.

3.2.1 Analyze the economic conditions required for implementing ESG investment

Stable financial support and sustainable business models lay a solid foundation for ESG investments, which are typically reflected in changes in ROA and ROE. Enterprises with higher ROA and ROE usually have stronger internal capital and more efficient operation management capabilities, enabling them to allocate resources over the long term to ES investment without compromising the achievement of short-term goals. Financial flexibility significantly promotes the improvement of ESG performance in strategic emerging enterprises, and the results remain robust and reliable after multiple robustness tests [16]. This study emphasizes that enterprises with strong ESG performance can enhance the positive cycle between ESG investments and financial performance. Companies with high ROA and ROE can better undertake ESG investments, and the implementation of ESG will further enhance the asset return capability.

3.2.2 Analyze the technical conditions required for implementing ESG investment

Unilever has utilized data-driven methods to achieve and optimize its sustainability status in terms of greenhouse gas emissions. As Wang, H. discussed, Unilever utilizes technologies such as supply chain analysis, prediction, and compliance checks, based on existing sustainable development standards and KPIs, to enable Unilever to monitor emission data throughout the entire supply chain and achieve the tracking and realization of ESG goals [17]. These technologies effectively measure and quantify carbon emissions and resource usage, which are crucial for the success of ES investment. This provides strong evidence that technology has established the fundamental conditions for ESG investments.

3.2.3 Analyze the legal and regulatory conditions required for implementing ESG investment

Legal regulations and supervision are also crucial for the feasibility of ESG investments. In recent years, governments around the world have successively introduced binding measures for ESG investment. By implementing accountability mechanisms, they aim to ensure the fairness and transparency of ESG investments. Companies that set the goal of ESG investment abide by and uphold laws and regulations. For instance, Unilever adheres to established guidelines such as the United Nations Global Compact and GRI standards, complies with EU regulations, meets the EU ES disclosure requirements, and voluntarily accepts supervision.

3.2.4 Analyze the human resource conditions required for implementing ESG investment

Furthermore, the human resources condition is the fundamental prerequisite for the successful implementation of ESG investments. The current market is facing a shortage of ESG professionals. Strategic talent cultivation focusing on ESG proficiency and executional excellence constitutes a pivotal imperative for enterprises to attain enduring strategic objectives. ESG investment not only requires the participation of the management team, but also demands an employee team that possesses ESG knowledge, high professional standards, and proficient operational skills. Unilever has provided targeted training courses for its employees in order to achieve its ESG goals, particularly in the areas of greenhouse gas emissions and supply chain sustainability. The company established an internal ESG working group, linking the performance of management with sustainable development, and emphasizing the significance of ESG for the organization.

The feasibility of ESG investment is not solely dependent on external conditions; rather, the internal human resource system plays a more significant role. Understanding how to stimulate employees' work enthusiasm and enhance team cohesion can help enterprises achieve their ESG investments more quickly and with greater benefits.

4. The Advantages and Disadvantages of ESG Investment

ESG investment stands out in business strategies thanks to its unique concepts and business models. ESG investment incorporates environmental, social and governance factors into the scope of investment management considerations, achieving an innovative perspective on financial returns and triggering a new trend in the global investment field.

4.1. Advantages of ESG investment

ESG investment has many advantages. This article conducts a detailed analysis from three aspects: resource management, green innovation, and risk management.

Firstly, ESG investment enjoys a significant competitive advantage in the field of resource management. ESG investment can effectively enhance the utilization rate of resources, prompting the upstream and downstream of the production chain to control the usage of energy, water and raw materials, and reduce unnecessary waste, thereby lowering production costs and increasing operating profits. According to the study by Mohammad and Wasiuzzaman, firm's sustainability efforts can help facilitate it to manage resources more efficiently and allow it to run its business effectively while providing solution to societal issues [18].

ESG investment has a positive impact on green innovation. ESG performance can increase the number of green invention patents; moreover, ESG performance moderates the relationship between R&D investment and green innovation performance [19]. Driven by the ESG investment goals, business managers are compelled to increase investment in green production technologies, establish automated supervision systems, and coordinate supervision of the upstream and downstream production processes. A good performance in social responsibility is conducive to attracting outstanding human resources and conducting cross-disciplinary green production activities, thereby promoting the green innovation of the enterprise.

Furthermore, ESG can help enterprises establish a framework for risk management. By actively managing the environment, society and governance aspects, enterprises can detect potential risks as early as possible, promptly formulate response plans and solutions, and minimize the risks associated with laws and regulations to the greatest extent. This characteristic is particularly evident in the hotel management industry. For instance, in the aforementioned hotel case, due to the impact of the pandemic, the performance of the hotel industry has significantly declined and it has been difficult to increase profits. The research results show that ESG investment can enhance the efficiency of hotels. The world's leading Marriott International hotel has implemented ESG investment practices. It accurately predicted the devastating impact that the pandemic would have on the hotel industry and quickly formulated employee health protocols to enhance employee well-being, promptly

implemented safety measures to reduce the risk of employee infection. The company also provided material support to the local community, maintained its corporate reputation and gained the trust of its customers.

4.2. Disadvantages of ESG investment

For enterprises to make ESG investments, they should not only focus on the advantages but also take into account all the disadvantages. Although ESG investment can bring long-term benefits to companies, it also brings some opportunities and challenges, especially in the early stages of investment.

The first challenge is the excessively high cost at the beginning of the investment. Implementing ESG investment requires a stable source of funds, solid infrastructure, a reliable data collection system, and a team of trained employees with extensive knowledge of ESG. The initial investment of funds is huge, and small and medium-sized enterprises may find it difficult to smoothly achieve financial allocation that meets ESG standards. In this regard, obviously only large companies can demonstrate their advantages. According to the research by Khanchel and Lassoued on ESG disclosure, over time, social information disclosure will increase the cost of capital [20]. This also proves that over time, the costs associated with ESG investment disclosure will increase, posing a threat to the normal flow of funds for enterprises. When deciding to make ESG investments, the management of the enterprise must consider whether there is sufficient internal funds available to support the investment and ensure its long-term success. For SMEs with limited internal funds, joint procurement of renewable-energy certificates within industrial clusters can meaningfully dilute per-unit ESG compliance costs, with early pilots in selected textile hubs already showing tangible savings.

Secondly, environmental issues in various regions and intensified industry competition have exacerbated the difficulties faced by ESG investments. ESG investment has not always held a dominant position. In different regions, the complexity and diversity of laws and regulations make it difficult for multinational companies to adopt a unified ESG strategy. Meanwhile, competition in certain industries is becoming increasingly fierce. Small and medium-sized companies as well as emerging enterprises are challenging the positions of established enterprises, forcing these enterprises to focus on short-term financial performance while neglecting long-term sustainable development. As a result, the realization of ESG performance is affected.

Although ESG faces certain challenges, the long-term benefits it brings far outweigh these limitations, making it worthy for enterprises to actively explore and adopt. The ESG investment strategy should be encouraged, as it has positive impacts on both the enterprises themselves and society.

5. Conclusion

Answering the research questions in turn, this study finds: (1) Long-term, stable ESG investment significantly raises both ROA and ROE, confirming its role in enhancing profitability. (2) The magnitude of these gains is moderated by industry characteristics and firm size: carbon-intensive and highly leveraged SOEs experience smaller improvements, whereas resource-constrained SMEs can exhibit greater ROE elasticity. (3) While ESG improves reputation and lowers financing costs, its impact on short-term debt-repayment risk remains limited and can even reverse under high leverage due to cash-flow pressure. (4) ESG strengthens brand value and customer loyalty, yet these long-term benefits unfold over extended horizons.

Constrained by the short sample period and uneven industry coverage, these findings call for further validation. Future research should extend the time span, employ dynamic-panel or event-study methods, and examine how ESG influences additional metrics such as cash-flow volatility, Tobin's Q, and credit spreads across diverse institutional settings and firm scales. Overall, integrating ESG into strategic and financial planning offers firms a viable path to enhance value and achieve sustainable development.

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