The Impact of ESG Ratings on Corporate Debt Availability: Evidence from Malaysian Public Listed Companies

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Abstract. When making lending decisions, creditors are paying more attention to companies' Environmental, Social, and Governance performance in recent years as global ESG awareness has grown more widespread. Although many studies show that ESG ratings has a positive impact on corporate debt accessibility, there is little to no related studies of this phenomenon in the Malaysian context. Thus, the purpose of this paper is to investigate how ESG ratings affect Malaysian public listed companies' corporate debt accessibility. This paper uses data from Malaysian public listed companies ranging from 2021-2023 extracted from the Refinitiv Eikon database, and regression analysis is performed to evaluate how corporate debt accessibility is affected by ESG ratings. The research findings reveal that corporate debt accessibility is enhanced by ESG ratings. From the perspective of the three ESG pillars, although social responsibility increases corporate debt accessibility, environmental and corporate governance have no impact on corporate debt accessibility. This means that ESG investments improve a firm reputation, enabling better access to financing conditions and scale.

Keywords: Corporate debt availability, debt financing, creditors.

1. Introduction

Environmental, Social, and Governance (ESG) refers to the environmental, social, and governance aspects of a company's operations. Global awareness and attention of ESG performance is becoming ever more widespread. The public is becoming more observant of firms' ESG performance; according to a 2020 investor survey, 72% of investors will analyse in a detailed fashion the ESG performance of firms [1]. Regulatory bodies are also calling for financial institutions to focus on ESG-related issues, requiring them to include ESG-related risks in their corporate default risk assessment process [2]. This shows that creditors have already started to shift from financial indicators to ESG's multidimensional factors when making lending decisions. Businesses nowadays must actively invest in improving their ESG performance to obtain a greater amount of financing to ensure their ability to procure working capital, encourage business expansion, and secure the sustainability of business operations. This trend compels businesses to incorporate ESG performance improvements as part of their core strategy.

Current research points out that the strong subjectivity of ESG information strengthens the information asymmetry between creditors and the firm, which lowers the credibility of the firm [3]. Therefore, firms must enhance their ESG performance and improve the transparency of their operations, to reinforce trust between creditors and companies via reducing the level of information asymmetry between them [3]. Active participation in ESG-related efforts conveys to creditors the firms' willingness to undertake ESG responsibilities and display to them their risk management capabilities and sustainability of operations, which amplifies their reputation and credibility, enabling them to achieve better financing amounts [4].

From the perspective of the three ESG pillars, the passing of the Climate Risk Management and Scenario Analysis (CRMSA) policy by the Malaysian Central Bank in 2022 requires firms to extend their participation in enhancing environmental responsibilities. High participation in social responsibility shows the strong stance of the firm in upholding social responsibilities, enabling it to gain wider societal support [4, 5]. An effective corporate governance framework discourages opportunistic behaviour from senior management, decreases agency costs, and conveys to creditors

that their strong operational efficiency and firm resources are put to good use [6]. Strong investments in each ESG pillar can enhance the firm's reputation and since reputation also works as a supervision tool, firms are compelled to maintain their level of ESG performance, maintain the amount and quality of ESG disclosures to maintain their positive image, and achieve consistency in obtaining good financing agreements [7].

This paper presents the following two hypotheses derived from the theories outlined previously:

H1: ESG rating has a positive impact on corporate debt accessibility.

H2: Individual ratings of the E, S, and G pillars have a positive impact on corporate debt accessibility.

Although there is much literature related to the subject, there is little attention paid to the Malaysian context. Thus, the purpose of this paper is to examine the Malaysian market, to determine whether ESG ratings improve the corporate debt accessibility of Malaysian public listed companies' (PLCs); to discuss the strategic value of ESG investments in an era of elevated ESG awareness. This paper analyses the influence of ESG ratings on the debt accessibility of PLCs in mid-sized economies, offering fresh insights into the relationship between ESG ratings and firm performance. This paper collects data from the Refinitiv Eikon database pertaining to the data of Malaysian PLCs from 2021-2023, which is then used to conduct descriptive analytics, correlation analytics, regression analytics, and robustness tests to examine and discuss how ESG ratings influence the debt accessibility of firms.

2. Research Design

2.1. Data Source and Sample Selection

This paper employs data from Malaysian PLCs ranging from 2021 to 2023, all extracted from the Refinitiv Eikon database. After removing financial companies and all companies with missing key variables, a total of 651 observations were obtained. To alleviate the influence of outliers on the regression outcome, all continuous variables were winsorized at the 1st and 99th percentiles.

2.2. Main Variables

Table 1. Main variables and their method of measurement

Type of Variable	Symbol of Variable	Name of Variable	Method of Measurement
Dependent Variable	DebtAccess	Corporate debt accessibility	(Year-end total liabilities – Total liabilities at beginning of the year)/Total Assets
Independent Variables	ESG	ESG rating	LSEG ESG Combined Score
	E	E rating	LSEG Environmental Pillar Score
	S	S rating	LSEG Social Pillar Score
	G	G rating	LSEG Governance Pillar Score
Control Variables	Size	Firm Size	ln (Total Assets)
	FAR	Fixed Asset Ratio	Fixed Assets/Total Assets
	Cash	Cash-to-Assets Ratio	Cash and cash equivalents/Total Assets
	ROA	Return on Assets	Net profit/Total Assets
	ROE	Return on Equity	Net profit/Total Equity
	Growth	Growth Rate	(Current year revenue-Previous year revenue)/Previous year revenue
	BOD	Board Size	Number of Board members
	Age	Firm Age	ln (2025 – Year of incorporation)
	Shariah	Compliance with Shariah Laws	Shariah Compliant=1; Non-Shariah Compliant=0

The dependent variable is corporate debt accessibility (DebtAccess) [8]. The independent variables are the London Stock Exchange Group (LSEG) ESG Combined Score and the E, S, and G pillar scores [9, 10]. To minimize the influence of other variables on the regression outcomes, some control variables are introduced into the model [11]. Table 1 describes all the variables used in this paper, their symbols, and how they are measured.

2.3. Model Specification

The following models were developed to examine how corporate debt accessibility is affected by ESG ratings:

$$DebtAccess_{it} = \beta_0 + \beta_1 ESG_{it} + \beta_k \sum Controls_{it} + \alpha_i + \lambda_t + \varepsilon_{it} \quad (1)$$

$$DebtAccess_{it} = \beta_0 + \beta_1 E_{it} + \beta_k \sum Controls_{it} + \alpha_i + \lambda_t + \varepsilon_{it} \quad (2)$$

$$DebtAccess_{it} = \beta_0 + \beta_1 S_{it} + \beta_k \sum Controls_{it} + \alpha_i + \lambda_t + \varepsilon_{it} \quad (3)$$

$$DebtAccess_{it} = \beta_0 + \beta_1 G_{it} + \beta_k \sum Controls_{it} + \alpha_i + \lambda_t + \varepsilon_{it} \quad (4)$$

Controls refers to this paper's control variables. α stands for industry fixed effects (FE), λ stands for year FE, and ε stands for the error term. Model (1) is used to test H1, while Models (2), (3), and (4) are used to test H2.

3. Results

3.1. Descriptive Statistics

Table 2. Descriptive statistics

Variable	N	Mean	Stdev	Min	Max
DebtAccess	651	-0.006	0.064	-0.212	0.201
ESG	651	45.131	17.664	12.761	84.337
E	651	34.823	21.882	1.532	86.090
S	651	47.843	21.179	9.017	90.115
G	651	52.797	21.556	8.180	93.657
Size	651	20.055	1.460	16.816	23.644
FAR	651	0.493	0.208	0.053	0.944
Cash	651	0.085	0.083	0.002	0.445
ROA	651	0.044	0.076	-0.210	0.310
ROE	651	0.089	0.176	-0.382	0.989
Growth	651	0.081	0.318	-0.675	1.460
BOD	651	8.138	1.895	5.000	14.000
Age	651	3.372	0.541	1.946	4.477
Shariah	651	0.811	0.392	0.000	1.000

The descriptive statistics results are shown in Table 2. The mean, minimum and maximum values of DebtAccess are -0.006, -0.212 and 0.201, respectively, which indicates that the debt accessibility of Malaysian PLCs is not high. Besides that, their debt accessibility is shrinking. The mean of ESG is 45.131. According to LSEG's ESG grading system, the grade of ESG performance of Malaysian PLCs is around C+, belonging to the medium-low scale. The standard deviation of ESG is 17.664, showing that there is a large variance in ESG performance among Malaysian PLCs. This could be due to differences in available resources that can be used for investing in ESG matters, or due to varying awareness and attention towards ESG issues among Malaysian PLCs. From the perspective of ESG's pillars, the mean ratings of E, S, and G are 34.823, 47.843, and 52.797, respectively. This indicates that Malaysian PLCs perform the best in terms of corporate governance, followed by social responsibility, and lastly, environmental responsibility. This could be due to environmental responsibility needing vast amounts of resources, its slow rate of return, and difficulty in measuring

investment results. Social responsibility needs fewer resources and has a faster rate of return. Corporate governance requires the least amount of investment, and its performance can be measured by the firm's degree of compliance with the Malaysian Code of Corporate Governance (MCCG), greatly reducing its measurement difficulty. The standard deviation of each dimension ranges between 21-22, showing that there is not much difference between these pillars' ratings between Malaysian PLCs.

3.2. Correlation Analysis

This paper has also performed correlation analysis between DebtAccess and the other main variables. The findings indicate there is a positive significant correlation between ESG and DebtAccess at the 10th percentile. Although this supports H1, it is not a strong correlational relationship. However, in contrast to H2, S and DebtAccess have a significant positive correlation at the 5th percentile, but both E and G's correlation with ESG are statistically insignificant. As for the correlation results of the control variables, Growth and DebtAccess have a positive and significant correlation, which explains that growth-stage firms require more resources to support business expansions and to support the increase in demand for working capital during business expansions. Age and DebtAccess have a significant negative correlation, which means the larger the firm age, the lower their debt accessibility. This might be because as firms become older, their standing in the market becomes stronger, which means that their operational income flows become more stable and growth opportunities are lessened, ultimately reducing the need for debt financing.

3.3. Regression Analysis

3.3.1 The relationship between ESG ratings and corporate debt accessibility

Table 3. Impact of ESG, E, S, and G ratings on corporate debt accessibility

	(1)	(2)	(3)	(4)
Variables	DebtAccess	DebtAccess	DebtAccess	DebtAccess
ESG	0.0004**			
	(0.0002)			
E		0.0002		
		(0.0001)		
S			0.0004***	
			(0.0002)	
G				0.0001
				(0.0001)
Controls	Yes	Yes	Yes	Yes
Constant	0.0357	0.0273	0.0391	0.0047
	(0.0417)	(0.0420)	(0.0412)	(0.0382)
Industry FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	651	651	651	651
R-squared	0.0631	0.0583	0.0663	0.0569

Note: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$, numbers in the brackets are robust standard errors.

The regression results between ESG alongside their pillars and DebtAccess are shown in Table 3, where it is shown that ESG's regression coefficient is 0.0004 and, at the 5th percentile, statistically significant; the regression results are more significant than the results from the correlation analysis done previously. This shows that the debt accessibility of firms improves significantly alongside the firms' ESG performance. It can be inferred that creditors will account for firms' ESG performance when deciding on lending to firms. Firms with good ESG performance will have better public image, and send signals regarding efficient usage of firm resources, which enhances the creditors' confidence

in the firm, enabling firms to obtain lenient lending agreements with creditors, extending their debt size. Hence, H1 is accepted.

3.3.2 The relationship between E, S, and G pillar scores and corporate debt accessibility

From Table 3, the regression coefficients for E, S, and G are 0.0002, 0.0004, and 0.0001 respectively. S has a 1% significant regression coefficient, but E and G's regression coefficients are not statistically significant, which supports the correlation analysis done in the previous section. This shows that social responsibility can increase a firm's debt accessibility; however, corporate governance and environmental responsibility has no positive influence on firms' debt access. The difference in results could be that it takes more capital to invest in environmental responsibility, which causes resource misallocation in core business activities, thus lowering business performance. The degree of environmental responsibility performance is difficult to measure, and its authenticity is difficult to verify, which diminishes its usefulness for creditors in lending decisions. Social responsibility requires relatively fewer resources and can quickly establish a positive impression for the firm, enhancing its reputation and legitimacy, strengthening creditors' trust in the firm, consequently widening the firm's financing size. The implementation of the MCCG could be the reason behind the results for G, as it enforces stricter corporate governance guidelines, which improve business performance. Stronger corporate governance weakens the need for external financing, and to avoid becoming highly leveraged, management will stick to utilising internal financing for daily operational needs, as external financing weakens the firm's financial flexibility. Therefore, H2 is partially accepted.

3.4. Robustness Tests

3.4.1 Changing independent variables

The independent variables shall be changed to assess the baseline regression's robustness. The ESG Combined Score Grade (ESG Grade) shall be used to replace the ESG ratings and their individual pillars' ratings. According to LSEG's ESG grading system, the entity's ESG performance shall be graded in correspondence to their rating, of which there are twelve grades, ranging from D- to A+. If the grade is D-, D, or D+, then ESG Grade=1; if the grade is C-, C, or C+, then ESG Grade=2; if the grade is B-, B or B+, then ESG Grade=3; if the grade is A-, A, or A+, then ESG Grade=4. The E, S, and G variables shall be treated in the same manner as the ESG rating, of which the new variables are E Grade, S Grade, and G Grade, respectively. Table 4 column (1) reveals that the ESG and S results are significant. The regression is robust, although the result for S is less significant than the baseline regression results. Therefore, H1 is accepted, while H2 is partially accepted.

3.4.2 Addition of missing control variables

Default risk (Defaultrisk), a new dummy variable shall be added to the regression model to evaluate the baseline regression's robustness. The firm's leverage shall serve as the proxy variable for determining whether the firm has default risk; should the firm's leverage be greater than or equal to its median (0.2806), then the firm is considered to have default risk, thus Defaultrisk=1; otherwise, Defaultrisk=0. The results for both ESG and S are still significant as seen in Table 4 column (2); they show the same level of significance as the results in Table 3, strengthening the robustness of the outcome. Hence, H1 is still accepted, while H2 is still partially accepted.

3.4.3 Lagged variables

The reason why firms have wide debt accessibility is due to their satisfactory operational performance, which lowers their non-payment risk, which subsequently boosts their capacity to participate in ESG-related initiatives; and it is not the opposite, where the debt financing ability of firms is not enhanced by firms' participation in ESG initiatives. This indicates that corporate debt accessibility and ESG ratings exhibits reverse causality. To avoid this issue and demonstrate that the baseline regression is indeed robust, the independent variables shall be lagged by one period for robustness testing. Table 4 column (3) indicates that the ESG and S results are still significant. Although the result for S is less significant than the baseline regression results, the results remain robust. Therefore, H1 is still accepted, while H2 is still partially accepted.

Table 4. Robustness test outcomes

	(1)		(2)		(3)
Variables	DebtAccess	Variables	DebtAccess	Variables	DebtAccess
ESG_Grade	0.0101**	ESG	0.0004**	L.ESG	0.0004**
	(0.0041)		(0.0002)		(0.0002)
E_Grade	0.0039	E	0.0002	L.E	0.0003
	(0.0032)		(0.0001)		(0.0002)
S_Grade	0.0082**	S	0.0004***	L.S	0.0003*
	(0.0034)		(0.0002)		(0.0002)
G_Grade	0.0026	G	0.0001	L.G	0.0002
	(0.0027)		(0.0001)		(0.0001)
Controls	Yes	Controls	Yes	Controls	Yes
Industry FE	Yes	Industry FE	Yes	Industry FE	Yes
Year FE	Yes	Year FE	Yes	Year FE	Yes

Note: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$, numbers in the brackets are robust standard errors.

4. Conclusion

Using a sample of Malaysian PLCs from 2021 to 2023, this study investigates whether ESG ratings enhance the accessibility of corporate debt. The findings indicate that corporate debt accessibility is positively impacted by ESG ratings. Diving into each of the ESG pillars, social responsibility is found to benefit corporate debt accessibility, but environmental responsibility and corporate governance does not affect corporate debt accessibility. The findings remain consistent after conducting several robustness tests. The results show that active efforts in improving ESG ratings and social responsibility performance convey the message that firms account for the social impact of their operations when planning operational activities, thus making suitable adjustments to their method of operations such that they benefit communities, which enables firms to expand their potential scale of financing. Based on these findings, this paper recommends that the relevant Malaysian authorities further improve and tighten corporate ESG disclosure standards, especially on corporate governance and environmental responsibility. Additionally, it is advised to strengthen the scrutiny of business operations' effects on the environment, society, and corporate governance. The authorities can reward firms that actively disclose ESG information or firms that have displayed improvements in their ESG performance, while simultaneously penalising firms that fabricate ESG disclosures, to encourage businesses to actively adjust their business practices. This is to minimise their potentially negative social impacts and encourage businesses to actively upgrade their ESG reporting methods. The differences in ESG ratings' influence on the debt accessibility between state-owned and non-state-owned companies are not explored in this paper; hence, future research should explore this subject to enhance the comprehensiveness of this study.

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