

# Integrating ESG Strategy into Socially Responsible Investment Decisions: A Literature Review

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## Abstract

Conscious investors embrace investments with not just financial but also social and environmental benefits. Investment made with a positive and cautious approach considering financial and social benefits is termed as Socially Responsible Investment (SRI). The Environment, Social and Governance (ESG) factors seem to be significant criteria while making socially responsible investment decision by the investor as they believe that their investment has a potential to address environmental and social issues. Nations, businesses, and investors across the world promote SRI, to tackle global issues such climate change, food security, global health, by incorporating ESG practices and strategies. SRI gained substantial importance and momentum post 2008 financial crisis. The study analyses the significance of incorporating ESG variables into SRI investment decision of the investors and the effect of ESG strategies on financial performance of SRI portfolios. The study employs a comprehensive literature review based on research papers, articles, and reports, to evaluate the benefits and challenges associated with integration of ESG criteria into investment strategies. The study contributes to the existing literature on SRI and integration of ESG practices towards sustainable development and there by provides valuable suggestions to policymakers, financial institutions, and researchers.

**Keywords:** Socially Responsible Investment, Environmental, Social and Governance, Investment Strategy, Social Impact

## 1. Introduction

The practise of incorporating environmental, social, and governance (ESG) factors into investment evaluation and

decision-making is known as socially responsible investing (SRI) and recently SRI has acquired increasing prominence and focus, and the value of SRI holdings has increased significantly (The Global

Sustainable Investment Alliance, 2019). By ensuring that funds are obtained and allocated in an efficient and responsible manner, investors play a critical role in the global drive to achieve sustainable development goals (UNPRI, 2017).

ESG strategy acts as a connect between sustainable development and responsible investing. SRI aims to promote environmentally responsible practices and has a beneficial effect on society through the inclusion of ESG concerns into investment decisions. The ideas of SRI and sustainability are often integrated to highlight the linked nature of business success, environmental protection, and social responsibility.

Institutional and retail investors (Sood, Pathak, Jain, & Gupta, 2023) are considering ESG aspects for investing though being a new concept in developing economy like India. Investors support businesses that actively strive towards achieving sustainable development goals, knowing that such an investment benefits the environment, society, and their money also. To promote long-term growth, a wide spectrum of market participants, including institutional and private investors, evaluate the environmental impact of their investments.

(Senadheera et al., 2021) Sustainable growth is directly tied to ESG investing, although it is challenging to achieve, these areas of ESG identified by analysts tend to significantly impact company's financial performance positively. The ESG factors seem to be significant criteria while making socially responsible investment decision by the investor as they believe that their investment has a potential to address environmental and social issues.

(SEBI, May,2021) Environmentally and socially responsible businesses are in high demand among investors and other stakeholders also regard ESG as a step towards

a more sustainable economy. ESG issues have recently gained attention on a global scale, further company's success based on sustainable ESG standards is now reported on at the same level as its financial and operational performance, taking this into account.

Most people believe that ESG data is more likely to disclose a company's weaknesses than its competitive advantages. Since there are no universally acknowledged reporting standards, it is difficult to compare ESG data from different sources, hence considered as a major challenge associated with ESG data (Amel-Zadeh & Serafeim, 2018).

Considering the incremental prominence of SRI and ESG philosophy, the current study aims to evaluate existing literature and analyze the significance of incorporating ESG information in decision criteria of investors, and the drawbacks of ESG data. The conclusion emphasizes theoretical implications, as well as the scope for future research and implications for stakeholders and businesses in terms of improving socially responsible investments.

## 2. Literature Review

### 2.1. The Nexus of SRI and ESG

Increased awareness of climate change, corporate governance crisis, and rising demands for corporate social responsibility have all contributed to the 21st century's significant expansion of socially responsible investment. The Principles of Responsible Investments of United Nations (UNPRI) was introduced in 2006 to provide a framework for integrating ESG factors into investment practices. The PRI with global network of signatories, include

asset proprietors, investment managers, and service providers committed to responsible investing. Investments that are socially responsible have a particularly important place in a global context that is concerned with the preservation of valuable and scarce resources (Tripathi, & Bhandari, 2014).

The UNPRI is committed to work with members for maintaining the minimum standards and extend helping hand to them towards principles of responsible investment. By the end of March 2021, the total AUM of all 3826 PRI members increased from US\$103.4 trillion to over US\$121 trillion, an increase of 17% (UNPRI, 2017).

SRI techniques screen assets that promote long-term investments using ESG factors in addition to financial data. SRI strategies use ESG variables to provide better long-term performance. The new SRI strategy, also known as sustainable investment, is popular in Europe than in the United States (The Global Sustainable Investment Alliance, 2019).

Members of GSIA have cited those fiduciary obligations as a primary incentive for sustainable investment, which is an indication that SRI is becoming more acceptable to a wider audience than it was in previous years. Concerns over the state of the environment have also served as a driving force, particularly in the wake of Climate Change highlighted (The Global Sustainable Investment Alliance, 2019).

## 2.2. Significance of ESG Data in Investor Investment Decision

(Young, 2013) highlights that institutional investors place more importance to market participation than market departure, and they frequently pursue this engagement in

an implicit manner, through communication. Governance issues, including succession planning and compensation, come in at the top of the priority list for this engagement, followed by environmental considerations and then occupational, health, and safety issues.

(Allianz Global Investors, 2010) Investors, both institutional and retail, are expressing a growing need for greater transparency and consideration of ESG concerns, that pave way to the emergence of sustainable investment practices around the world.

Evidence from (Williams, 2007) Australia, Canada, Germany, UK, and USA provide that a substantial proportion of investors consider the social and environmental behavior of a company while making investment decisions and show that investor qualities as consumers, as well as their overall attitude towards enterprises' social objectives, influence their investment decisions. However, it appears that financial rewards and demographic features have minimal influence on SRI decision.

(Beloskar, & Rao, 2022) supports the superior management paradigm and demonstrates that ESG investments perform better in times of crisis and ESG rankings have a favorable impact on both regular and emergency stock return volatility (van Duuren, Plantinga, & Scholtens, 2016) adds to the evidence of ESG's positive impact on investment performance as well as insights into the perspectives and behaviors of ESG managers who incorporate ESG data into investment decisions. ESG investors favor company-level Governance analysis, which impacts management quality.

(Pedersen, Fitzgibbons, & Pomorski 2021) demonstrates that the maximum responsible investment decision is achieved at a relatively high level of ESG when

substituted by governance mechanism. A slight decline in SR is the result of elevating ESG, proving that moral objectives may be attained at low cost and that investors have preferences about ESG and use ESG information to get investment intelligence decisions.

(Tripathi, & Bhandari, n.d.) In 2007 India launched ESG index for the first time to evaluate ESG practices on the basis of objective criteria rather than subjective. The index uses an original and cutting-edge approach that measures a firm's ESG practices and converts them into a scores or metrics that is then used to rank each company against its Indian market competitors.

(Thanki et al., 2022) finds that environmental concerns influence not only investor views but also investor investment intentions. Enterprises can concentrate on providing proper social and environmental disclosures in their reporting practices to safeguard investors' specific values about sustainability, which may also help investors make educated investment decisions.

(Sparkes, & Cowton, n.d.) considerations social, environmental, and ethical (SEE) appear to be important in decisions on investments, along with conventional financial information. Positive and negative SEE considerations seem to influence investing decisions in many ways, and investors are willing to bear the resulting financial performance tension.

(Jonwall et al., 2022a) Responsible investors have better knowledge of SRI than conventional investors as SR investors take into account company's environmental/sustainability report prior to forming an investment decision. Responsible and traditional investors are concerned about broad ESG issues.

(Tripathi, & Bhandari, 2014) found the facts that out of numerous indices such as

GREENEX and ESG performed very well when compared with the CNX 500, NIFTY, and SENSEX stock indices in terms of financial returns and risk and a few risk-adjusted criteria reinforcing India's need for social investment. Ethical investors in India may create strong, high-performing portfolios using a portfolio of socially conscious stocks and recommend that mutual funds and other investment fund managers create SR stock-investment programs so that small investors in India get access to information on SRI options and funds.

(Jonwall et al., 2022b) inferred that knowledge of sustainability indices, understanding of responsible investing, ESG funds, willingness to invest in sustainable investments, and perception of global concerns, all seem to have a significant influence on responsible investment decision of Indian retail investors.

### 3. Research Methodology

The present study is descriptive study based on comprehensive literature review taken from quality databases like Wiley, Scopus, Springer, Emerald, and Google Scholar. The keywords used to find the literature was socially responsible investments, SRI/ESG strategies, ESG Practices, SRI and ESG, SRI and Sustainable development. Academic articles, empirical research papers, strategic reports were used for analysing the benefits and challenges of incorporating ESG factors into socially responsible investment and further conclusions were drawn. The articles were selected on the basis of objectives of the study firstly to understand the concepts of SRI and ESG secondly how and why investors consider ESG factors before investing and thirdly the limitations of ESG information. The study adds to the existing knowledge on SRI and the incorporation of ESG practices to achieve sustainable development

**TABLE 1.** Summary of significant articles included in the study.

S. No	Author (year)	Journal	Theme	Research type	Findings
1	Tripathi, & Bhandari, n.d. 2014	FIIB Business Review	Evolution and growth of SRI and ESG funds	Exploratory	SRI funds performed better
2	Beloskar, & Rao, 2022	Asia Pacific Financial Markets	Performance of ESG funds during Crisis times	Exploratory	Positive performance and value addition to investors
3	Van Duuren et al., 2016	Journal of Business Ethics	Significance of ESG in investment decisions	Exploratory	ESG investing is significant and aligns fundamental investing
4	Daugaard, 2020	Accounting & Finance AFAANZ	Understand the significance and theme of ESG investing	Systematic Literature review	Contribution to literature
5	Pedersen et al., 2021	Review of Finance	Integration of ESG on the portfolios of UNPRI signatories	Exploratory	Committed role of signatories to ESG
6	Indriastuti, & Chariri, 2021	Cogent Business and Management	CSR and Green investment and its impact on Financial and sustainable performance	Exploratory	Financial performance seems to be in significant
7	Nejla Ould Daoud Ellilli, 2022	Corporate Governance	Impact of ESG on Financial reporting and investment efficiency	Exploratory	Positive significant of ESG on financial reporting
8	Widyawati, 2020	Business Strategy and investment	Importance of ESG information in SRI	Systematic literature review	ESG enables SRI and sustainable development
9	Senadheera et al., 2021	Sustainable development	The evaluation of ESG metrics and propose a framework	Exploratory	E pillar is significant in ESG metrics
10	Sood et al., 2023	Managerial Finance	Significant ESG criteria and sub criteria for investors	Empirical	ESG information has important relevance in investor investment decision
11	Amel-Zadeh, & Serafeim, 2018	Financial Analysts Journal	ESG information and its importance to investors	Empirical	Significant for risk analysis but are subjected to ESG information limitations.
12	Sciarelli et al., 2021a,b	The TQM Journal	The role of SRI and ESG and sustainable development	Empirical	ESG strategies in SRI portfolios are significant for sustainable development

and may provide useful recommendations to policymakers, financial institutions, and researchers.

## 4. Discussion

### 4.1. Drawbacks and Limitations of ESG Data

It is understood well that socially responsible investments or sustainable investments are imperative for achieving sustainable development and the significance of ESG strategies and ESG practices adopted by firms holds crucial for investment decisions among institutional and retail investors. (Camilleri, 2020) adds that the involvement of stakeholders and the making of sustainable investments by responsible firms can assist such businesses enhance their bottom lines while also addressing the issues that exist in their communities and the society. But it is also identified that there are various impediments that stand in the way of socially responsible investment and sustainable development. The problem is the lack of ESG investing understanding among Indian investors as ESG investing and ESG funds are nascent in India. Indian investors are paying greater attention to companies with a social conscience. ESG will probably alter long-term investing practices worldwide. Market return volatility is inversely correlated with ESG rankings during times of crisis stimulating ESG investment in emerging economies like India (Beloskar, & Rao, 2022).

There is a need for more effective and consistent information of the environmental and societal implications of SRI to measure its impact, promote investor choice, and accelerate the movement of finance towards sustainability. (Sciarelli Mauro et

al., 2021a,b) Long-term sustainability is enhanced by the prominence of ESG inclusion and its associated consumption shift in investing behavior towards a finer ethical and sustainable approach. Institutional investors may benefit from the incorporation of ESG variables into their investment options by reducing their potential exposure to market volatility and facilitate the value and benefits of implementing SRI tactics like ESG inclusion and positive or negative screening exclusion.

(Charlo, Moya, & Muñoz 2015) While social responsibility is vital, it is not always practiced. Most businesses claim that financial worries push them to be socially responsible, yet the research found little evidence of this. Although responsible investment results have no negative consequences, socially responsible indexes and institutional investors in financial markets do not differentiate between responsible and conventional investment methods. Even though most research indicates that CSR practices do not negatively impact corporate outcomes, financial performance measures reveal no additional benefits for ethical organization.

(Jonwall et al., 2022b) Fund managers must consider the ESG SRI challenges while creating new investment vehicles. Investors in India have shown much interest in SRI and a propensity to tolerate lower returns, but consider the high risk associated with SRI channels as a significant barrier to socially responsible investing.

Fiduciary obligation (Jansson, & Biel, 2011) is being prudent and responsible with financial outcomes regardless of social and environmental concerns. Institutional investors prioritise social and environmental issues less than beneficiaries. Investment institutions may underestimate ESG difficulties for their benefiter sand over value

financial returns due to value discrepancy, and underestimate SRI product demand.

(Busch, Bauer, & Orlitzky 2016) Since sustainable investment is a reality and requires a methodological reorientation towards a long-term paradigm. Banks and investors are important drivers of sustainable development and improving ESG assessments is also crucial to realizing their full potential. These measures lay the groundwork for opening new channels via which sustainable investments may advance sustainable development.

(Senadheera et al., 2021) Environmental (E) scoring may not be a good tool for greening the financial industry because it's hard to compare, the metrics are biased, many environmental elements are mixed, rating providers use different methods, and may not be of high-quality data sets. To improve the ESG pillar, issues concerning varying scope and evaluation standards must be fixed to promote sustainable finance and development.

ESG rating agencies (Pu, Chankoson, Dong, & Song 2022) sprung as an answer to the requirement of SR investing players for trustworthy information on societal performance of the business but were found to be uneven and ununified in their measurement of ESG.

(Cruz & Matos, 2023) Investors need transparent, consistent, ESG investment information but have trouble getting sustainability information on ESG metrics since most frameworks lack openness, reliability, consistency, materiality. Lack of materiality, validity, trustworthiness, and accessibility are among the obstacles to using ESG data (Jonsdottir, Sigurjonsson, Johannsdottir, & Wendt (2022)).

The results (Jonwall et al., 2022b) identified a lower awareness of SRI among investors, and most of them agreed that ESG

factors are important in investment decision and were inclined towards SRI options, at the same time were unwilling to tolerate low returns. It is also identified that along with low returns, absence of a tax advantage, lack of data and metrics on SRIs, and low liquidity as significant barriers to SR investment. Investment opinions are highly dependent on the knowledge of SR funds and ESG information, and their propensity to SR investment options, and according to the findings there is a need to raise investor knowledge on the concepts and advantages of ESG investing in developing economies.

(SEBI, May,2021) The SEBI Circular dt November 2015 specified a structured reporting format for ESG criteria for listed companies known as BSRB. The purpose of Business Responsibility and Sustainability Reporting (BRSR) is to provide numerical and uniform information on ESG criteria for the purpose of facilitating comparisons across firms, industries, and time. With the aid of such disclosures, better investment decisions can be made. The BRSRs will facilitate businesses' interactions with their stakeholders by requiring them to consider factors besides profits.

## 5. Conclusion

Socially responsible investing and ESG strategies gained prominence as there is a requirement for ethical and sustainable investments and to accelerate sustainable development. Investors can aid responsible businesses by addressing environmental considerations like climate change and resource conservation, social ones like human rights and labor practices, and governance practices through their investments. SRI and ESG investing promotes sustainability, social good, and corporate

accountability and improves long-term financial performance. But SRI and ESG information suffer from inconsistent reporting and lack of standards making ESG performance comparisons across firms and industries problematic. Strong ESG guidelines and investment selection are essential for responsible investment. Sustainability, corporate responsibility, and non-financial issues drive socially responsible investing decision of investors, benefitting the society and business. Standardization of ESG metrics, data quality, trade-offs between financial returns and sustainability objectives, require careful considerations to strengthen ESG frameworks and establish transparency to promote ESG and SRI and move towards sustainable development and economy. ESG investment strategy is becoming more popular but are subjected to drawbacks such as lack of standardisation in ESG metrics and data availability and quality may be restricted if businesses do not disclose comprehensive and accurate ESG information leading to inconsistent reporting and the lack of established criteria further hinder data comparability.

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