Journal DOI: 10.36713/epra1013 | SJIF Impact Factor (2024): 8.431 ISSN: 2347-4378
EPRA International Journal of Economics, Business and Management Studies (EBMS)
Volume: 11 | Issue: 7 | July 2024 -Peer-Reviewed Journal

ESG INTEGRATION IN FINANCIAL SECTORS: A CASE OF SUSTAINABILITY INVESTMENT STRATEGIES

Aishwarya R Shetty[1] & Dr. Neethu Suraj[2]

[1] *Research Scholar, Institute of Management and Commerce, Srinivas University, Mangalore, India*
ORCIDID:0009-0005-5974-7947

[2] *Associate Professor, Institute of Management and Commerce, Srinivas University, Mangalore, India, ORCIDID: 0000-0002-4443-383*

Article DOI: https://doi.org/10.36713/epra17662
DOI No: 10.36713/epra17662

ABSTRACT

Purpose: *The integration of Environmental, Social, and Governance (ESG) factors in the financial sector, aiming to comprehend the present tactics, evaluating the efficiency of sustainability investment, and recognizing the challenges and opportunities that financial firms face while implementing ESG criteria.*

Design/Methodology/Approach: *A semi-systematic review methodology, looking at secondary data from a variety of released papers and articles collected through platforms such as Google Scholar, ResearchGate, Shodh Ganga, and Springer. This method provides an in-depth analysis of trends and difficulties in ESG integration in the financial sector.*

Findings: *The financial institution under consideration has greatly improved its business image and trademark value by implementing ESG standards. Integrating ESG principles has helped to manage risks, improve long-term financial viability, and meet the demands of regulators. However, the organization faces obstacles such as data quality issues, the credibility of ESG claims, and the need to combine short-term financial goals with long-term sustainability objectives. The case study emphasizes the potential for new financial products, as well as the importance of strong regulatory frameworks to facilitate ESG integration.*

Practical Implications: *The results suggest that uniform reporting standards and complete ESG compliance procedures are essential for successful ESG integration. The financial institution should integrate ESG into its essential business strategies to improve productivity and stakeholder trust. Also, regulatory settings must promote innovation and standardization of ESG practices, as well as raise market knowledge and educate consumers about the financial ramifications of these principles.*

Originality/Value: *This work provides a thorough examination of the current level of ESG integration in the financial sector, emphasizing both the benefits and problems. It makes practical ideas for enhancing ESG practices and emphasizes the need for more study to better understand the long-term effects of ESG on financial success.*

Paper Type: *Case study*

KEYWORDS: *ESG Integration, Sustainability Investment Performance, Sustainability in Finance*

1. INTRODUCTION

The financial services sector has increasingly realized the importance of integrating Environmental, Social, and Governance (ESG) factors into investment tactics. This move reflects a broader understanding that sustainability business procedures are not just ethical imperatives but also critical components of long-term financial performance. As investors and stakeholders demand are in higher transparency and accountability, financial institutions have been adapting their strategies to integrate ESG criteria, thereby aligning investment procedures with the global drive towards sustainability.[1]ESG integration involves reviewing companies based on their environmental impact, social ethical behavior, and governance practices. This method gives an in-depth examination of potential risks and opportunities that may not be apparent through traditional financial analysis alone. After taking factors such as carbon emissions, labor practices, and board diversity, investors can better predict a company's future performance and resilience.[2] Several key trends highlight the importance of ESG in financial services: regulatory bodies worldwide are tightening requirements for ESG disclosure, pushing companies to be more transparent about their sustainability practices; and there is an increasing amount of evidence suggesting that businesses with robust ESG profiles tend to outperform their peers over the long term, both in terms of stock performance and risk mitigation.[3]

Journal DOI: 10.36713/epra1013 | SJIF Impact Factor (2024): 8.431 ISSN: 2347-4378
EPRA International Journal of Economics, Business and Management Studies (EBMS)
Volume: 11 | Issue: 7 | July 2024 -Peer-Reviewed Journal

2. REVIEW OF THE LITERATURE

The numerous works on ESG Integration in Financial Sectors:

SI.NO	AREAS	CONTRIBUTION	REFERENCE
1.	ESG Investment Strategies	ESG investment methods show considerable differences in governance characteristics across regions, interconnected environmental and social agendas, and varying performance outcomes in established versus emerging economies	Meira, E.,Arias Fogliano de Souza Cunha, F., Orsato, R. J.,Miralles-Quirós, M. M., & Miralles-Quirós, J. L. (2022). [4]
2.	Corporate Governance	Corporate governance in the financial services sector focuses on theoretical perspectives, regulatory monitoring, and compliance effectiveness, prompting more academic and practitioner research.	Handley-Schachler, M., Juleff, L., & Paton, C. (2007).[5]
3.	Sustainability Reporting	It emphasizes the importance of sustainability reporting on financial performance in Australian and New Zealand listed firms, citing industry type and kind of sustainability report as key determinants driving abnormal returns.	Eddy, K., & Gordon, L. W. (2010). [6]
4.	Regulatory Landscape	The regulatory framework is critical for integrating ESG aspects into investment strategies because it offers established norms, ensures compliance, and promotes duties. Continuous efforts are needed to meet increasing issues in ESG investment and sustainability goals.	Ran Xiao, Jiaqi Deng, Yuting Zhou, & Meng Chen. (2023). [7]
5.	Stakeholder Engagement	Finance performs crucial roles in encouraging broad acceptance of ESG management by building ESG measurement infrastructures improving ESG-linked financial intermediaries, and facilitating ESG valued trading in markets to successfully align financial and societal goals.	Park, Y. S., & Lee, H. S. (2023) [8]
6.	Innovation in Financial Products	Investigating technology's impact on financial products and investor views, with a special focus on Blockchain's promise as a model for future financial systems.	Shah, T. M. (2024). [9]
7.	ESG Metrics and Ratings	Studies found that excellent ESG performance in financial institutions is associated with solid governance procedures and transparent openness, whereas worse performers generally demonstrate deficiencies in ethical conduct and consumer openness.	Mandas, M., Lahmar, O., Piras, L., & De Lisa, R. (2023). [10]

3. OBJECTIVES:

- To identify current strategies and practices in ESG integration within the financial sector.
- To evaluate the effectiveness of sustainability investment strategies.
- To determine difficulties and possibilities for financial institutions adopting ESG criteria

4. METHODOLOGY

This study uses secondary data in order to provide extensive details on the issues and trends of the ESG integration within the financial sector. This semi-systematic review is carried out by using the variety of published papers and articles from various sources such as google scholar, research gate, Shodh Ganga, springer.

5. ESG INTEGRATION

In the recent years, ESG guidelines have grown significantly in various sectors, boosting corporate reputations, handling risk, and sustainability while addressing obstacles like data quality and greenwashing. The rise of ESG-focused financial products and global regulations to standardize reporting have encouraged companies to integrate

environmental social and governance into core strategies, influencing investors attitudes towards responsible ethical investing and fostering new markets dynamics [11]. Integrating ESG principles creates obstacles in data quality, regulatory adaptation, and market awareness but provides opportunities for sustainability investments and new business growth. Financial institutions should enhance data transparency, educate market participants, and leverage technology to drive social sustainability [12]. Environmental Social and Governance ideas within financial institutions is mainly driven by regulatory mandates and evolving shareholder preferences, which are transforming into operational practices and decision-making processes. The present research focus on how ESG integration and sustainability reporting are reshaping the financial sector, increasing sustainable ethical choices, and meeting the demands of the people. [13] The transition "best-in-class ESG Factor Integration" has been driven by more data disclosure, more improved research, and integration with traditional investment methodologies, expanding ESG integration despite initial underperformance in exclusionary strategies.[14] Integrated approaches to Sustainable Investment improve ESG risk management and sustainability outcomes, emphasizing the need for strategies that address broader challenges and align with global sustainability goals.[15] The importance of integrated economic and ecological initiatives support sustainable equitable goals and mitigate environmental degradation and social disparities in the region.[16] Integrating ESG principles helps banks to handle risks, innovate with products like green loans, and enhance customer goodwill, despite regulatory challenges and calls for more comprehensive ESG laws.[17]

6. SUSTIANABILITY IN FINANCE:

The systematic analysis evaluated in 181 publications across 110 journals from 1999 to 2019, finding six essential sub-themes in sustainable finance, with climate finance and sustainable banking recognized as pivotal areas for future research. The author concluded that these areas indicate a strong academic and industry interest in addressing environmental and social impacts through financial mechanisms.[18] Integrated Financial and Sustainability Reporting combines financial and non-financial aspects to offer a broad view of organizational performance, enhancing transparency and getting together with stakeholder demands for insights into social, environmental, and financial impacts. This approach, led by countries like South Africa, aligns corporate practices with global sustainability goals and societal expectations.[19] The financial intermediaries such as cooperative banks, SRI funds, ESG analysis, microfinance, Islamic finance, and Fintech, as well as the role of ethical and sustainable finance in sustainable development, emphasizing green finance's impact on reducing environmental risk and inequality. It concludes with a call for policy measures to promote global sustainable footprint certification.[20] The adoption of sustainable finance models in EU nations within the OECD demonstrates a substantial positive association between meeting the Sustainable Development Goals (SDGs), improving social fairness, environmental stewardship, and economic resilience.[21]Traditional finance study techniques are being reconsidered in light of the rise of sustainable finance, with a focus on qualitative changes in financial activities. It identifies basic contradictions in current financial descriptions and provides methodological approaches to promote a more inclusive approach to incorporating sustainability into finance research and education.[22] A "value-driver adjustment" (VDA) strategy to incorporating sustainability into financial decision-making, improving business models, competitive positions, and value drivers, and so strengthening and extending the relationship between companies and their shareholders.[23]

7. SUSTAINABILITY INVESTMENT PERFORMANCE:

Firms that invest in environmental programs can improve financial performance by lowering environmental concerns, aligning with customer preferences, and creating long-term economic benefits.[24] A new quantitative model discovered that sustainability improves investment performance in the German DAX from 2003 to 2012, notably during market crises, implying a strong commercial justification for socially responsible investment (SRI) strategies.[25] The impact of sustainability on Australian property investment decisions, advocating for an integrated approach that takes economic, social, environmental, policy, and regulatory considerations into account when shaping future investment plans and portfolio management in the industry.[26] Integrating ESG principles increases shareholder value by resulting in superior risk-adjusted returns for ESG-focused funds, which correlate with lower cost of capital and market outperformance, with governance being the most important factor, followed by environmental and social aspects, despite neutral or mixed results from SRI funds.[27] Green and CSR investments positively impact financial and sustainable performance in Indonesian manufacturing, emphasizing alignment with community values and the need for broader research.[28] From 2013 to 2017, sustainable indices such as TRESGDX and TRESGEX performed similarly to typical MSCI indexes, demonstrating their potential as replacements in portfolio strategies and performance benchmarking for financial managers and executives.[29]

8. ESG ADOPTION CHALLENGES:

One of the significant hurdles to ESG adoption identified in the study is the inconsistent integration of sustainability practices across different business contexts and industries in the Indian service industry. This includes variations in technology preparedness, varied levels of commitment to comprehensive sustainability methods beyond simple

Journal DOI: 10.36713/epra1013 | SJIF Impact Factor (2024): 8.431 ISSN: 2347-4378
EPRA International Journal of Economics, Business and Management Studies (EBMS)
Volume: 11 | Issue: 7 | July 2024 -Peer-Reviewed Journal

measures like paper reduction, and issues related with the environmental impact of remote work, such as increasing energy usage in home offices.[30] Identifying critical hurdles to ESG adoption in organizations and investigating their interrelationships using the modified Delphi approach and the model, combining expert opinions with the Z number and RDWGA approach, and making recommendations for successful ESG implementation.[31]

9. FINANCIAL SECTOR ESG OPPORTUNITIES AND BARRIERS:

The present research looks into how environmental, social, and governance (ESG) concerns influence venture capital (VC) investment decisions. Based on interviews with 11 venture capitalists, the study evaluates causes, implementation techniques, and hurdles to ESG adoption. The findings show that ESG is becoming increasingly important for long-term investments, driven by performance benefits and a limited number of partners. Challenges include a lack of common frameworks and resources. Policy and industry support could help smaller VC firms embrace ESG practices, while entrepreneurs could address ESG criteria to match with investor interests.[32]

10. CURRENT TREND:

Robust ESG data and effective data management are crucial for financial services to meet sustainability goals, with Data Mesh offering a transformative framework to address data complexities and enhance collaboration. This approach ensures innovation and compliance, driving progress in ESG and sustainability initiatives. [33] a positive correlation between growth in the economic and sustainability performance in Asia, highlighting the significance of integrated economic and environmental regulations. This supports sustainable development goals and helps mitigate the damage of the environment and social inequalities in the region.[34] Inflation and economic instability will pose difficulties to sustainability activities in 2023, but the sustainable debt market and new disclosure regulations will help to progress sustainability goals in the face of escalating ESG litigation and a renewed focus on climate, water, biodiversity, and human rights issues.[35] In an effort to satisfy decarbonization goals, large Indian corporations are rapidly introducing internal carbon pricing, power optimization, net-zero agreements, and green initiatives.[36]

11. SWOC ANALYSIS OF ESG INTEGRATION IN THE FINANCIAL SECTOR:

STRENGTHS	• ESG practices improve corporate reputations and brand value in banking, manufacturing, technology, and healthcare.
	• Integrating ESG helps to manage environmental, social, and governance risks, hence enhancing long-term stability.
	• The development of ESG-focused financial products such as indices, ETFs, green bonds, and derivatives meets expanding demand while also effectively managing ESG risks.
	• Regulatory efforts are standardizing ESG reporting while also promoting compliance and transparency.
WEAKNESSES	• Problems with data capture and quality impede efficient ESG integration and reporting.
	• Difficulties in validating the legitimacy of ESG claims across corporations, compromising credibility and trust.
	• Influence of ESG practices on financial performance is difficult to quantify due to varied approaches and indicators.
OPPORTUNITIES	• ESG-focused financial products expand, new market dynamics emerge.
	• Adequate regulatory regimes can encourage widespread adoption of ESG practices and the standardization of reporting formats.
	• Raising market knowledge and education about ESG ideals can lead to greater adoption and understanding among stakeholders.
	• Advancement in the technology
CHALLENGES	• Costs involved with developing strong ESG compliance standards and reporting methods.
	• Sector faces unique hurdles in adopting and integrating ESG concepts effectively.
	• Struggle to balance short-term financial aims with long-term sustainability objectives.

12. FINDINGS

- Environmental, social, and governance (ESG) practices significantly improve corporate image and trademark value in a variety of industries, including banking, production, technology, and healthcare.

- Integrating ESG helps handle environmental, social, and governance risks, which promotes long-term financial stability.
- The development of ESG-focused investment strategies such as indexes, ETFs, green bonds, and derivatives meets rising demand while effectively mitigating ESG risk.
- Regulatory actions are increasingly aimed at simplifying ESG reporting, fostering compliance and transparency.
- ESG integration fosters new market dynamics and opens up opportunities for innovative financial services and goods.
- Issues with gathering information and quality impair effective ESG integration and reporting.
- Difficulties in determining the accuracy of ESG claims across corporations endanger credibility and confidence.
- The influence of ESG practices on financial performance is difficult to measure due to the variety of techniques and indicators used.
- Companies may incur major expenses when developing robust ESG standards and reporting techniques.
- Balancing short-term financial goals with long-term sustainability objectives can be difficult for businesses.

13. SUGGESTIONS:

- Support for consistent reporting standards that enhance transparency and comparability across industries.
- Assist companies to include ESG into their basic business plans for long-term performance and stakeholder trust.
- Implement stronger ESG compliance procedures and demanding reporting mechanisms to reduce risks and improve performance.
- Execute more study in order to comprehend the long-term and nonlinear implications of ESG on financial success.
- Investigate integrated socioeconomic and ecological strategies to help achieve sustainable development goals.
- Engage market participants about ESG ideals and their financial implications in order to increase acceptance and comprehension.
- Support for regulatory settings that foster creativity and standardization in ESG practices.
- Facilitate collaboration among stakeholders, such as regulators, investors, and firms, to advance ESG integration and sustainability objectives.

14. CONCLUSION

Implementing ESG factors into core financial sectors improves corporate reputation, risk management, and long-term financial stability. However, challenges such as data quality, credibility of ESG claims, and maintaining short-term and long-term goals persist. The study demonstrates the need for uniform reporting standards, broad compliance procedures, and solid regulatory frameworks to promote ESG practices. Integrating ESG into basic business objectives can boost productivity and trust among stakeholders, but more study is needed in order to comprehend its long-term financial implications and promote sustainable development goals.

REFERENCE

1 *Eccles, R. G., Ioannou, I., & Serafeim, G. (2014). The Impact of Corporate Sustainability on Organizational Processes and Performance. Management Science, 60(11), 2835-2857.*
2 *Google Scholar*
3 *Friede, G., Busch, T., & Bassen, A. (2015). ESG and financial performance: aggregated evidence from more than 2000 empirical studies. Journal of Sustainable Finance & Investment, 5(4), 210- 233.Google Scholar*
4 *Revelli, C., & Viviani, J. L. (2015). Financial performance of socially responsible investing (SRI): What have we learned? A meta-analysis. Business Ethics: A European Review, 24(2), 158-185.Google Scholar*
5 *Meira, E., Arias Fogliano de Souza Cunha, F., Orsato, R. J., Miralles-Quirós, M. M., & Miralles- Quirós, J. L. (2022). The added value and differentiation among ESG investment strategies in stock markets. Business Strategy and the Environment. Advance online publication.1(1), 17-20 Google Scholar*
6 *Handley-Schachler, M., Juleff, L., & Paton, C. (2007). Corporate governance in the financial services sector. Corporate Governance, 7(4), 475-484. Google Scholar*
7 *Eddy, K., & Gordon, L. W. (2010). The effect of sustainability reporting on financial performance: An empirical study using listed companies. Journal of Asia Entrepreneurship and Sustainability, 6(2), 19-42.Google Scholar*
8 *Ran Xiao, Jiaqi Deng, Yuting Zhou, & Meng Chen. (2023). Analyzing contemporary trends in sustainable finance and ESG investment. Law and Economy, 2(11), 44–52. Google Scholar*

9 *Park, Y. S., & Lee, H. S. (2023). The roles of finance in ESG management. Asia-Pacific Journal of Financial Studies. Advance online publication.1(1), 27-36. Google Scholar*
10 *Shah, T. M. (2024). An empirical study on technological innovations of selected financial products: Perception of investors in Gujarat and Blockchain technology model (Doctoral dissertation). GLS University. Shodhganga@INFLIBNET*
11 *Mandas, M., Lahmar, O., Piras, L., & De Lisa, R. (2023). ESG in the financial industry: What matters for rating analysts? Research in International Business and Finance. Advance online publication.1(1),56-78.Google Scholar*
12 *Acar, E. (2024). ESG Integration into Financial Markets: A Comprehensive Exploration of Concepts and Implementation. Çağ Üniversitesi Sosyal Bilimler Dergisi, 20(2), 133-147. Google Scholar*
13 *Wang, L. (2024). Challenges and opportunities of ESG integration in financial operations.Modern Management Science & Engineering, 6(1), 162-170 https://doi.org/10.22158/mmse.v6n1p162*
14 *Yu, X. (2023). Integration of ESG in Financial Institutions: A Study on the Impact of Sustainability Reporting. International Journal of Management Research and Global Economy, 4(5),468-472.GoogleScholar*
15 *Roselle, P. (2016). The evolution of integrating ESG analysis into wealth management decisions. Journal of Applied Corporate Finance. Advance online publication.2(1),157-167 Google Scholar*
16 *Folqué, M., Escrig-Olmedo, E., & Corzo Santamaría, T. (2021). Sustainable development and financial system: Integrating ESG risks through sustainable investment strategies in a climate change context. Sustainable Development, 29(2), 356-368.Google Scholar*
17 *Wang, L. (2024). Investigating the integration of ESG factors into financial markets and its influence on sustainable economic growth in emerging Asian economies. Journal Name, 8(5), Article ID 3911. Google Scholar*
18 *Borodako, A. (2023). ESG integration in banking: A qualitative study on the impact of regulation on banks' operations.3(1),222-240 Google Scholar*
19 *Jayaram, R., & Singh, S. (2020). Sustainable finance: A systematic review. International Journal of Indian Culture and Business Management, Advance online publication.1(1), 341-365. Google Scholar*
20 *Oza, K. (2023). A study on integrated financial and sustainability reporting in selected listed companies of India (Doctoral dissertation, GLS University). Shodhganga@INFLIBNET*
21 *Ferri, G., & Acosta, B. A. (2019). Sustainable finance for sustainable development. LUMSA University, Rome, Italy.1(1), 20-50. Google Scholar*
22 *Ziolo, M., Bak, I., & Cheba, K. (2021). The role of sustainable finance in achieving Sustainable Development Goals: Does it work? Technological and Economic Development of Economy, 27(1), 45-70. Google Scholar*
23 *Lagoarde-Segot, T. (2018). Sustainable finance: A critical realist perspective. Research in International Business and Finance.1(1),89-90. Google Scholar*
24 *Schramade, W. (2016). Bridging sustainability and finance: The value driver adjustment approach. Journal of Applied Corporate Finance, 28(2), 39-46. Google Scholar*
25 *Singal, M. (2014). The link between firm financial performance and investment in sustainability initiatives. Cornell Hospitality Quarterly, 55(1), 19-30. Google Scholar*
26 *[25] Peylo, B. T., & Schaltegger, S. (2014). An equation with many variables: unhiding the relationship between sustainability and investment performance. Journal Name, 2(1)110-126.Google Scholar*
27 *[26] de Francesco, A. J., & Levy, D. (2008). The impact of sustainability on the investment environment. Journal of European Real Estate Research, 1(1), 72-87.Google Scholar*
28 *[27] Fulton, M., Kahn, B., & Sharples, C. (2012). Sustainable Investing: Establishing Long-Term Value and Performance. Deutsche Bank AG. 1(1),89-110.Google Scholar*
29 *[28] Indriastuti, M., Chariri, A., & McMillan, D. (Reviewing editor). (2021). The role of green investment and corporate social responsibility investment on sustainable performance.2(1),57-80. Google Scholar*
30 *[29] Jain, M., Sharma, G. D., & Srivastava, M. (2019). Can Sustainable Investment Yield Better Financial Returns: A Comparative Study of ESG Indices and MSCI Indices. Risks, 7(1), 15.Google Scholar*
31 *[30] Efthymiou, L., Kulshrestha, A., & Kulshrestha, S. (2023). A Study on Sustainability and ESG in the Service Sector in India: Benefits, Challenges, and Future Implications. Administrative Sciences, 13(7), 165.Google Scholar*
32 *[31] Liou, J. J. H., Liu, P. Y. L., & Huang, S. W. (2023). Exploring the key barriers to ESG adoption in enterprises. Sustainable Accounting and Standards, 7(1), 200066. Google Scholar*
33 *[32] Lange, E. M., & Ghotbedini Banadaki, N. (2024). ESG consideration in venture capital: Drivers, strategies and barriers. Studies in Economics and Finance. Advance online publication.1(1),789-889Google Scholar*
34 *[33] Aliyeva, L., & Alkemade, T. (2024, June 25). Powering sustainability and ESG in financial services with product thinking and Data Mesh. Articles: Data Mesh, Sustainability, Article. https://www.thoughtworks.com/en-in/insights/articles/sustainability-esg-financial-services-product-thinking-data-mesh*
35 *[34] Morningstar. (n.d.). ESG investing trends: Financial advisors depend on research they trust. The growing interest in sustainability demands it. Retrieved from https://www.morningstar.com/views/esg-investing-trends*

36 *[35] S&P Global. (n.d.). Key sustainability trends that will drive decision-making in 2023. Retrieved from https://www.spglobal.com/esg/insights/featured/special-editorial/key-sustainability-trends- that-will-drive-decision-making-in-2023*

37 *[36] Kalia, C., & Saha, S. (2022, June 27). How ESG megatrends and opportunities are shaping our future. EY Insights. https://www.ey.com/en_in/climate-change-sustainability-services/how-esg-megatrends-and-opportunities-are-shaping-our-future*