

ESG AND COMPANY MARKET VALUE: THE MEDIATING EFFECT OF FINANCIAL PERFORMANCE

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Abstract: *This study explores the correlation between ESG performance and company market value, with a particular emphasis on the mediating role of financial performance within listed firms in Vietnam. The main goal of this study is to analyze a representative sample of 199 publicly listed companies in Vietnam from 2019 to 2023. The findings reveal that ESG positively impacts market value by enhancing financial performance, particularly profitability. By investigating the relationship between ESG performance and company market value, alongside the mediating role of financial performance, this study contributes meaningfully to existing knowledge. Focusing on financial performance as a mediator, the research offers deeper insights into how ESG factors influence market value. The findings hold practical relevance for various stakeholders, including investors, policymakers, and corporate managers. By emphasizing the role of ESG in driving both financial performance and market value, the study highlights the necessity for companies to embed ESG considerations into their strategic decision-making to improve long-term sustainability, reduce risks, and attract socially responsible investors. Additionally, the study provides actionable recommendations for stakeholders such as investors and policymakers, reinforcing the importance of integrating ESG principles into business and regulatory frameworks.*

• Keywords: ESG, company market value, financial performance, mediating effect.

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1. Introduction

Research on Environmental, Social, and Governance (ESG) and the market value of companies is essential as ESG has become a crucial factor in evaluating financial performance and the comprehensive value of businesses. Companies committed to sustainable practices often outperform their peers in stock market performance and accounting measures over time (Eccles, Ioannou, and Serafeim, 2014). This superior performance can be attributed to better stakeholder engagement, improved innovation processes, and robust governance mechanisms, all highlighting the strategic advantage of integrating sustainability into business operations.

Studying the mediating role of financial performance is necessary to better understand how ESG impacts a company's market value. Factors such as reputation, customer loyalty, and operational efficiency can be enhanced through ESG commitments, leading to long-term financial improvements (Flammer, 2015). This research helps to elucidate how ESG factors can lead to improvements in financial metrics, which can reflect in market value and investor confidence.

Previous research has highlighted the intricate relationship between ESG performance and company value, often examining the mediating role of financial performance indicators. For instance, studies by Dhaliwal, Tsang, and Yang (2011), as well as Jo and Harjoto (2011), utilized comprehensive meta-analyses across various regions and industries, demonstrating that ESG factors significantly influence financial performance, which in turn contributes to company market value.

The present study investigates the relationship between ESG performance and key financial metrics of listed companies in Vietnam. It seeks to analyze financial indicators to understand how ESG performance aligns with the financial health and stability of these firms. Additionally, the study examines the connection between ESG performance and market value, aiming to determine how ESG factors are reflected in the valuation of these companies. Using quantitative methods, the research empirically explores the factors influencing the interplay between ESG performance, financial performance, and market value. The data, spanning the period from 2019 to 2023, is sourced from financial reports, reputable

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industry publications, and market data. The primary methodologies include the Ordinary Least Squares (OLS) model, Fixed-Effect Model (FEM), Random-Effect Model (REM), and Feasible Generalized Least Squares (FGLS) approach. By employing these methods, the study aims to uncover the direct impact of ESG performance on financial outcomes and market valuation, while also clarifying the mediating role of financial performance in this relationship.

The next parts of this paper include: (ii) Literature Review on ESG, Company Market Value, and Financial Performance, (iii) Research Methodology, (iv) Research Results and Discussions, and (v) Conclusions and Recommendations.

2. Literature Review

The relationship between ESG and company market value

Research has consistently demonstrated a positive link between ESG practices and company market value. Studies by Darnall et al. (2010) and Delmas & Pekovic (2018) highlight how environmentally sustainable practices boost business performance. Aragon-Correa et al. (2008) and Ambec & Lanoie (2008) emphasize the importance of aligning environmental strategies with organizational goals to enhance competitiveness. Margolis & Walsh (2003) provide strong evidence that firms with robust CSR commitments outperform peers in market valuation and shareholder value creation. Hubbard & Lenne (2013) underscore the evolving nature of CSR, emphasizing adaptability and proactive engagement with social and environmental issues.

Overall, ESG factors significantly influence market value by driving financial performance, improving operational efficiency, and strengthening competitive positioning, ultimately reflecting firms' ability to meet stakeholder expectations and adapt to market dynamics.

The Mediating Effect of Financial Performance

Financial Performance and ESG

According to Hart (1997) and Elkington (1997), businesses must go beyond basic environmental initiatives to achieve long-term sustainability. Hart (1997) advocates for a shift from superficial environmental actions to a comprehensive

rethinking of business operations and strategies. He introduces the "sustainable value framework," which positions sustainability as more than a matter of compliance or risk management, it becomes a key driver of innovation and financial growth. Similarly, Elkington (1997) presents the concept of the Triple Bottom Line (TBL), which expands traditional success metrics to include social and environmental performance alongside financial results. He emphasizes that businesses should evaluate their success based on their impact on people, the planet, and profit.

At the same time, Barney's (1991) resource-based theory highlights the importance of a firm's resources and capabilities in achieving sustained competitive advantage. Within the framework of Environmental, Social, and Governance (ESG) considerations, this theory suggests that firms excelling in ESG performance often possess unique and valuable resources. These resources not only help address environmental and social challenges but also create economic value and reduce risks.

Financial Performance and Company Market Value

The relationship between financial performance and market value can be understood through two primary theories: absolute valuation and relative valuation. Absolute valuation, or intrinsic valuation, suggests that a company's true value is based on its fundamental characteristics and expected future cash flows. As explained by James Chen (2020), the intrinsic value is calculated by discounting the company's projected future cash flows to their present value using an appropriate discount rate. This theory assumes that while market prices may temporarily deviate from intrinsic value, they eventually align over time. Analysts applying absolute valuation typically use methods like discounted cash flow (DCF) analysis, dividend discount models (DDM), or residual income models to determine a company's intrinsic worth based on its financial performance and growth potential.

In contrast, relative valuation assesses a company's market value by comparing it with similar companies or market benchmarks. According to Alicia Tuovila (2024), this approach evaluates a company's value relative to its peers using financial metrics such as the price-to-

earnings (P/E) ratio or other valuation multiples. Relative valuation operates on the premise that investors often make decisions based on comparative metrics, particularly in efficient markets where information is readily available and quickly reflected in stock prices.

3. Research Methodology

3.1. Research model and research hypothesis

This study turns its focus towards other financial performance indicators, drawing from established research findings. Notably, the metrics of return on equity (ROE), total asset turnover (TAT), and net profit growth (NPG) emerge as commonly utilized benchmarks in evaluating the financial health and operational efficiency of listed companies.

ESG, Profitability and Company Market Value

First, the model of the impact of ESG performance on the company's market value is constructed:

$$\text{Model 1: } MV(it) = \alpha_{10} + \alpha_{11} * ESG(it) + \alpha_{12} * Size(it) + \alpha_{13} * Lev(it) + \alpha_{14} * TAT(it) + \alpha_{15} * NPG(it) + \alpha_{16} * GDP(it) + \epsilon_{1it}$$

Where is the $MV(it)$ value of company i in year t , α_{10} is a constant term and ϵ_{1it} is a residual term, α_{11} represents the influence coefficient of ESG performance on market value and $\alpha_{12} - \alpha_{16}$ represent the influence coefficient of each control variable on company value.

Second, the model of the impact of ESG performance on profitability is constructed:

$$\text{Model 2: } ROE(it) = \alpha_{20} + \alpha_{21} * ESG(it) + \alpha_{22} * Size(it) + \alpha_{23} * Lev(it) + \alpha_{24} * TAT(it) + \alpha_{25} * NPG(it) + \alpha_{26} * GDP(it) + \epsilon_{2it}$$

Where $ROE(it)$ is the return on total equity of company i in year t , α_{20} is a constant term, ϵ_{2it} is a residual term, α_{21} represents the influence coefficient of ESG performance on profitability, and $\alpha_{22} - \alpha_{26}$ represent the influence coefficient of each control variable on profitability.

Finally, a test model of the mediating effect of profitability is constructed:

$$\text{Model 3: } MV(it) = \alpha_{30} + \alpha_{31} * ESG(it) + \alpha_{32} * ROE(it) + \alpha_{33} * Size(it) + \alpha_{34} * Lev(it) + \alpha_{35} * TAT(it) + \alpha_{36} * NPG(it) + \alpha_{37} * GDP(it) + \epsilon_{3it}$$

Where is the $MV(it)$ value of company i in year t , α_{30} is a constant term and ϵ_{3it} is a residual term, and $\alpha_{33} - \alpha_{37}$ represent the influence coefficient of control variables (Size, Lev, TAT, Growth) on profitability.

Based on the above theories, this section proposes the following hypotheses:

H1: Improved ESG performance positively contributes to the enhancement of company market value.

H2a: Improved ESG performance positively influences profitability.

H3a: Profitability mediates the relationship between ESG performance and company market value..

ESG, Operational Capability and Company Market Value

$$\text{Model 4: } MV(it) = \beta_{10} + \beta_{11} * ESG(it) + \beta_{12} * Size(it) + \beta_{13} * Lev(it) + \beta_{14} * ROE(it) + \beta_{15} * NPG(it) + \beta_{16} * GDP(it) + \epsilon_{1it}$$

$$\text{Model 5: } TAT(it) = \beta_{20} + \beta_{21} * ESG(it) + \beta_{22} * Size(it) + \beta_{23} * Lev(it) + \beta_{24} * ROE(it) + \beta_{25} * NPG(it) + \beta_{26} * GDP(it) + \epsilon_{2it}$$

$$\text{Model 6: } MV(it) = \beta_{30} + \beta_{31} * ESG(it) + \beta_{32} * TAT(it) + \beta_{33} * Size(it) + \beta_{34} * Lev(it) + \beta_{35} * ROE(it) + \beta_{36} * NPG(it) + \beta_{37} * GDP(it) + \epsilon_{3it}$$

Where MV_{it} is the market value of company i in t , TAT_{it} is the total asset turnover of the company i in t , β_{10} , β_{20} , and β_{30} are constant terms. ϵ_{1it} , ϵ_{2it} , and ϵ_{3it} are residual, β_{11} said ESG performance coefficient, β_{21} represents the influence coefficient of ESG performance on TAT, and $\beta_{12} - \beta_{37}$ represent the control variables influence coefficient of the market value of the company.

The second set of hypotheses is further proposed:

H1: Improved ESG performance positively contributes to the enhancement of company market value.

H2b: Improved ESG performance positively influences operational capacity.

H3b: Operational capacity mediates the relationship between ESG performance and company market value.

ESG, Growth Capability and Company Market Value

$$\text{Model 7: } MV(it) = \gamma_{10} + \gamma_{11} * ESG(it) + \gamma_{12} * Size(it) + \gamma_{13} * Lev(it) + \gamma_{14} * ROE(it) + \gamma_{15} * TAT(it) + \gamma_{16} * GDP(it) + \theta_{1it}$$

$$\text{Model 8: } NPG(it) = \gamma_{20} + \gamma_{21} * ESG(it) + \gamma_{22} * Size(it) + \gamma_{23} * Lev(it) + \gamma_{24} * ROE(it) + \gamma_{25} * TAT(it) + \gamma_{26} * GDP(it) + \theta_{2it}$$

$$\text{Model 9: } MV(it) = \gamma_{30} + \gamma_{31} * ESG(it) + \gamma_{32} * NPG(it) + \gamma_{33} * Size(it) + \gamma_{34} * Lev(it) + \gamma_{35} * ROE(it) + \gamma_{36} * TAT(it) + \gamma_{37} * GDP(it) + \theta_{3it}$$

The Third set of hypotheses related to Growth Indicator is further proposed:

H1: Improved ESG performance positively contributes to the enhancement of company market value.

H2c: Improved ESG performance positively influences growth capacity.

H3c: Growth capacity mediates the relationship between ESG performance and company market value.

Variables measurement as follows: *MV*: Market value using P/B; *ESG*: Converted by the company's ESG rating; *ROE*= Net profit/ Common stockholders' equity; *TAT*= Net operating income/ Total average assets; *NPG*= Net profit growth/ Net profit of last year; *SIZE*= The natural logarithm of a company's average annual total assets; *LEV*= Average annual total liabilities/Average annual total assets; *GDP*= Total output/ Total population.

3.2. Research sample

Our study is based on a sample of 199 companies listed on the Ho Chi Minh Stock Exchange (HOSE) and the Hanoi Stock Exchange (HNX). These companies were selected based on the availability and completeness of their ESG data, ensuring the reliability and robustness of the analysis.

4. Research results and discussions

4.1. Descriptive statistics

Table 1. Descriptive statistics

Variables	Mean	Std. Dev.	Min	Max
MV	1,648492	1,03752	0,21	7,48
ESG	0,394603	0,1720211	0,05	0,74
ROE	0,1433047	,0941546	-0,07	0,6734
TAT	1,74196	1,526798	0,07	7,01
NPG	0,0718012	0,4561644	-0,9037	1,4984
Lev	0,4581106	0,2054745	0,02	0,91
SIZE	7,968667	1,614899	4,732464	14,6488
GDP	3856	314,342	3491	4284
Observations	995	995	995	995

Source: Calculated by the authors (2024)

Table 1 provides an overview of the descriptive statistics for the variables used in the analysis, covering the 995 observations over the period from 2019 to 2023. The dataset includes 199 companies listed on the Ho Chi Minh Stock Exchange and the Hanoi Stock Exchange, resulting in a total of 995 observations.

4.2. Correlation Analysis

Table 2 reveals that the highest absolute correlation coefficient between variables is 0,4817. Therefore, no significant multicollinearity issue

exists among the variables in the model developed in this study, enabling regression analysis to proceed in the subsequent steps.

Table 2. Pearson correlation analysis

	MV	ESG	ROE	TAT	NPG	Lev	SIZE	GDP
MV	1,0000							
ESG	0,0949	1,0000						
ROE	0,5001	0,0706	1,0000					
TAT	0,0098	-0,0295	0,1774	1,0000				
NPG	0,1080	0,0551	0,3827	0,0735	1,0000			
Lev	0,0074	-0,0493	-0,0605	0,3644	0,0226	1,0000		
SIZE	0,1951	-0,0679	0,0039	-0,1072	0,0345	0,4817	1,0000	
GDP	-0,1282	-0,0701	-0,1571	-0,0607	-0,1329	-0,0563	0,0729	1,0000

Source: Calculated by the authors (2024)

4.3. Regression Results

Regression analysis of the relationship between ESG performance and company market value

Table 3. The estimation results of the model (1), (4), (7)

VARIABLES	(1)	(4)	(7)
	MV	MV	MV
ESG	0,580***	0,433***	0,407**
	(0,184)	(0,160)	(0,162)
ROE		5,730***	5,346***
		(0,319)	(0,308)
TAT	0,0664***		-0,0208
	(0,0237)		(0,0214)
NPG	0,160**	-0,255***	
	(0,0699)	(0,0653)	
Lev	-0,912***	-0,391**	-0,321*
	(0,200)	(0,154)	(0,179)
SIZE	0,197***	0,157***	0,148***
	(0,0239)	(0,0195)	(0,0211)
GDP	-0,000458***	-0,000259***	-0,000229**
	(0,000102)	(8,95e-05)	(8,99e-05)
Constant	1,904***	0,601	0,611
	(0,430)	(0,380)	(0,384)
Observations	995	995	995
R-squared	0.094	0.312	0.302

Note: The values in parentheses (*), (**), (***) correspond to significance levels of 10%, 5% and 1%.

Source: Calculated by the authors (2024)

Using the OLS estimation method, the results from all three models show that the estimated coefficient for the ESG variable ranges from approximately 0,407 to 0,580, with all coefficients being statistically significant at the 1% level. These findings support Hypothesis H1, confirming that improvements in ESG performance enhance company market value. This is consistent with existing literature, such as Hammami's study (2015), which found that companies with strong ESG practices tend to have higher market values. Additionally, the results align with Maqbool and

Zameer (2019), who also identified a positive correlation between ESG performance and market value, suggesting that companies prioritizing sustainable and ethical practices are rewarded with higher market valuations.

Mediating Effect of Financial Performance on the relationship between ESG and Company Market Value

To validate hypothesis H2, equations (2), (5), and (8) were employed to investigate whether enhancements in ESG performance contribute to improvements in financial performance. The findings are displayed in Table 4 below.

Table 4. The estimation results of the model (2), (5), (8)

VARIABLES	(2) ROE	(5) TAT	(8) NPG
ESG	0,0267* (0,0156)	-0,365 (0,241)	0,0710 (0,0782)
TAT	0,0151*** (0,00200)		-0,00166 (0,0103)
NPG	0,0716*** (0,00592)	-0,0157 (0,0980)	
Lev	-0,105*** (0,0169)	4,180*** (0,230)	0,0729 (0,0864)
SIZE	0,00818*** (0,00202)	-0,363*** (0,0293)	0,00672 (0,0102)
GDP	-3,47e-05*** (8,62e-06)	0,000147 (0,000134)	-0,000106** (4,35e-05)
ROE		3,605*** (0,478)	1,804*** (0,149)
Constant	0,218*** (0,0364)	1,780*** (0,570)	0,109 (0,186)
Observations	995	995	995
R-squared	0,212	0,285	0,155

Note: The values in parentheses (*), (**), (***) correspond to significance levels of 10%, 5% and 1%.

Source: Calculated by the authors (2024)

A notable positive correlation is found between ESG performance and company profitability, supporting Hypothesis H2a. However, the relationship between ESG performance and operating capacity, as shown in Model (5), lacks statistical significance. This challenges the theoretical hypothesis, indicating that improvements in ESG performance may not significantly affect operating capacity. As a result, Hypothesis H2b is rejected, and Hypothesis H3b, which suggests that operational capability mediates the impact of ESG performance on market value, is also overturned.

The connection between ESG performance and growth capability, as analyzed in Model (8), shows

no statistically significant results. This challenges the hypothesis that ESG performance influences growth capability, leading to the rejection of Hypothesis H2c. Additionally, the failure of Hypothesis H3c suggests that growth capability may not mediate the relationship between ESG performance and market value.

Table 5. The estimated results of the model 3

VARIABLES	OLS	REM	FEM	FGLS
ESG	0,425*** (0,160)	0,219 (0,225)	-0,266 (0,303)	0,226** (0,111)
ROE	5,807*** (0,328)	3,294*** (0,370)	1,418*** (0,429)	4,336*** (0,242)
TAT	-0,0212 (0,0212)	-0,0343 (0,0320)	-0,0196 (0,0498)	-0,0222 (0,0146)
NPG	-0,255*** (0,0653)	-0,198*** (0,0490)	-0,0928* (0,0481)	-0,248*** (0,0306)
Lev	-0,303* (0,177)	0,244 (0,249)	2,101*** (0,351)	-0,185 (0,117)
SIZE	0,150*** (0,0210)	0,0674* (0,0355)	-0,825*** (0,111)	0,141*** (0,0143)
GDP	0,000256* **	-0,000324*** (6,18e-05)	-4,25e-06 (7,29e-05)	-0,000214*** (4,87e-05)
Constant	1,765*** (8,95e-05)	1,765*** (0,348)	7,217*** (0,731)	0,644*** (0,213)
Observations	995	995	995	995
Prob > F	0,0000	0,0000	0,0000	Wald chi2(7) = 505,57 Prob > chi2 = 0,0000
TESTING	TESTING VALUE			RESULT
Choosing between OLS and REM (Breusch - Pagan)	P-value= 0,0000			Choosing REM
Choosing between FEM and REM (Hausman)	P-value= 0,0000			Choosing FEM
Chosed Model				FEM
Heteroskedasticity	Chi2 (199) = 5,6e+05 Prob > chi2 = 0,0000			There is evidence of heteroskedasticity
Autocorrelation	F(1,198) = 18,590 Prob > F = 0,0000			There is evidence of autocorrelation

Note: The values in parentheses (*), (**), (***) correspond to significance levels of 10%, 5% and 1%.

Source: Calculated by the authors (2024)

Regarding Hypothesis H3a, which examines whether profitability mediates the effect of ESG performance on market value. The results from Model (3) are shown in Table 5. After conducting the Breusch-Pagan test, the P-value indicates heteroscedasticity, suggesting the use of the Fixed Effects Model (FEM) over OLS and REM models. However, FEM results were found to be biased due to issues with error variance and autocorrelation, so the Feasible Generalized Least Squares (FGLS) method was used for more reliable estimates.

The FGLS regression results confirm that improved ESG performance positively influences market value, partially through profitability. This supports Hypothesis H3a, indicating that profitability is a key pathway through which ESG impacts market value. Specifically, a 1% increase in ESG performance leads to a 0,226% increase in market value for Vietnamese companies. These findings align with previous studies by Dewi (2023) and Anser et al. (2018).

Furthermore, profitability, as measured by ROE, shows a significant positive effect on market value. A 1% increase in ROE corresponds to a 4,336% increase in market value, supporting previous research by Maditinos et al. (2011) and Almumani (2018). These results confirm that profitability mediates the relationship between ESG performance and market value.

5. Conclusions and Recommendations

This paper analyzes the relationships between ESG performance, financial performance, and company market value, using panel data from 199 listed companies across various industries. The study applies a mediation effect model to explore these interactions. Key findings include that improved ESG performance positively impacts profitability, suggesting companies with strong ESG practices are more profitable. However, ESG improvements do not significantly affect operational capacity or growth potential. The research also shows that enhanced ESG performance boosts market value, with profitability acting as a key mediator. In essence, companies with better ESG performance become more profitable, and this increased profitability drives higher market valuations.

Therefore, the research propose some recommendations for stakeholders. For listed firms, adopting robust ESG practices significantly enhances a company's reputation, making it more attractive to investors. Firms that demonstrate strong ESG performance often experience increased investor confidence and favorable market recognition. Financially, improved ESG practices can lead to enhanced profitability and higher market valuation. However, while ESG improvements boost profitability, they do not directly impact operational efficiency or growth rates. Companies must focus on integrating ESG considerations into their core strategies to achieve comprehensive business growth and efficiency. For investors, educating investors about the long-term benefits of ESG investments is crucial for making informed decisions. Recognizing the financial advantages of supporting companies with strong ESG practices helps investors shift their perspectives and prioritize sustainability in their portfolios. Transparent reporting on ESG efforts further builds trust, ensuring investors see a clear commitment to responsible governance. Investing in high ESG-performing companies

can lead to better financial outcomes, as these firms typically show higher profitability and increased market value. Finally, policy makers play a vital role in fostering a sustainable business environment by introducing incentives such as tax breaks and subsidies for exemplary ESG practices. These financial incentives lower the barriers for companies aiming to enhance their ESG efforts, promoting broader adoption of sustainable practices. Establishing and enforcing minimum ESG standards helps ensure a baseline level of corporate responsibility across the market. Additionally, national awareness campaigns and educational programs raise public and business understanding of ESG importance, driving a culture of sustainability. Public-private partnerships further encourage innovative solutions to ESG challenges, promoting collective action toward sustainability goals.

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