

The Empirical Examination of the Effect of Environmental, Social, and Governance (ESG) Performance on Enterprise Value: Focusing on Real Estate Agencies

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ABSTRACT

In the 21st century, modern production techniques and technological advancements have yielded remarkable development achievements, yet they are accompanied by challenges posed by energy and resource scarcity, ecological and environmental strain, and pressing social issues. Recently, the spotlight has shifted to environmental, social, and governance (ESG) factors, as negative social events have heightened public awareness. The impact of corporate ESG performance on society is significant, and the public's perception can, in turn, affect corporate profitability and overall value. As such, investors are increasingly realizing the importance of considering ESG metrics in their decisions. While ESG investment is still in its nascent stage domestically, it has garnered widespread attention and is rapidly gaining momentum. Indices and related derivative products themed around ESG, such as the ESG Beauty 50 index, have been launched on domestic exchanges like the Shanghai Stock Exchange and China Securities Index. Taking the real estate industry as a case study, this paper aims to accomplish the following through a combination of literature research and empirical analysis: Firstly, to assess whether ESG performance varies across companies with diverse characteristics (such as state-ownership status, enterprise size, and so forth) and explore its differential impact on enterprise value. Secondly, to raise awareness among company managers regarding the critical role of ESG performance in shaping the future sustainability and long-term value of their organizations.

KEYWORDS

ESG performance; Firm value; Real estate companies

1. SIGNIFICANCE OF THE RESEARCH TOPIC AND OVERVIEW OF ITS CURRENT STATUS WORLDWIDE

The concept of ESG integrates three key aspects: Environment, Social Responsibility, and Corporate Governance. Its genesis can be traced back to ethical and responsible investment strategies, as outlined by Michelson [1] and other scholars. Existing research primarily explores the impact of each individual dimension on corporate value, yet no consensus has been achieved at the macro level.

With regards to the environmental aspect, the prevailing view is that a company's environmental performance has a beneficial impact on its overall value. Hu Quying [2] echoes this sentiment, emphasizing the positive correlation between environmental performance and corporate value. Furthermore, Song [3] and his colleagues (2017) discovered a significant positive link between environmental management practices and subsequent financial performance.

Regarding social responsibility, opinions are more divided. Some studies indicate a positive correlation, whereas others suggest a negative one or no correlation at all. Yang Ziyue and Yin Jianguo [4] support the positive correlation hypothesis, whereas Vance [5] (1975) and Lerner [6] (1994) argue for a negative correlation. On the other hand, McWilliams and Siegel [7] maintain that social responsibility does not significantly affect corporate value.

Turning to corporate governance, Metrick [8] and his team (2003) found that companies with stronger shareholder rights tend to have higher Tobin Q ratios, reflecting a stronger market value relative to asset replacement costs. Liu Yinguo and Zhu Long's research [9] (2011) suggests that good corporate governance enhances a company's future financial security, leading to improved profitability and attracting investors willing to pay a premium for well-governed enterprises.

Additionally, several studies have shown that the impact of ESG performance on financial value is influenced by various micro-characteristics of enterprises, including industry nature. For instance, Cui et al.'s (2015) study on Chinese private enterprises revealed that larger enterprises' fulfillment of social responsibilities can sometimes reduce enterprise value, while Yang Wansu and Yang Shanlin (2016) observed that the relationship between social responsibility and corporate value is generally positive for large enterprises but negative for smaller ones. Industry nature also plays a role; Liu Wenwen and Duan Shengsen (2013) discovered that the environmental performance of state-owned enterprises has a more pronounced and direct effect on enhancing financial value. Conversely, Li et al. (2015) argue that state-owned enterprises may have less incentive to invest in social practices due to their entitlement to preferential treatment, thereby weakening the link between corporate social responsibility and financial performance. Industry type matters too; Iwata and Okada's (2011) analysis of Japanese manufacturing enterprises showed that reducing greenhouse gas emissions (indicating superior environmental performance) can boost the financial performance of clean industries but has less significant impact on polluting ones.

In conclusion, the relationship between ESG performance and corporate value remains inconclusive. This could be due to the varying development conditions of different types of enterprises across countries and inconsistencies in scholars' methodologies for calculating and measuring ESG factors. Most foreign studies predominantly concentrate on developed countries, leaving a notable void in research pertaining to emerging markets such as China. Within the domestic sphere, there is a tendency for studies to zero in on a single aspect of environment, society, or corporate governance, rather than offering a holistic analysis of the intricate relationship between ESG performance and corporate value. This is particularly evident in the context of specific industries within the tertiary sector, such as the real estate industry, where comprehensive research is scarce.

2. RESEARCH OBJECTIVES, KEY CONTENTS, AND PIVOTAL ISSUES TO BE ADDRESSED

This paper aims to delve into the intricate relationship between the ESG performance and enterprise value of prominent real estate enterprises. To accomplish this, it will conduct a comprehensive evaluation of these enterprises from three crucial perspectives: Environmental (E), Social (S), and Governance (G).

2.1. Research Content

To assess whether the ESG performance of Chinese real estate companies can enhance corporate value, this paper will gather data from leading listed real estate companies spanning the years 2020 to 2023. The study will meticulously explore the relationship between ESG performance and corporate value. Drawing from the research findings, the paper will formulate informed policy recommendations tailored to real estate companies, taking into account perspectives from enterprises, governments, and investors alike.

2.2. Key Issues

First, how is firm value influenced by ESG performance

Second, the different nature of enterprises, such as ownership structure and size, on the impact of ESG on firm value

3. RESEARCH METHODS, TECHNICAL ROUTE, EXPERIMENTAL SCHEME TO BE ADOPTED AND FEASIBILITY ANALYSIS

3.1. Literature Research Method

By reading relevant literature, this paper further understands and absorbs the related concepts involved in this paper, consults related academic achievements and recent research trends, and finds the shortcomings and unsolved problems among them. Combined with the purpose of this study, this paper summarizes its own research ideas and builds the corresponding basic structure.

3.2. Empirical Analysis

This paper will capture the data of listed leading real estate enterprises from 2020 to 2023, process and analyze the data, adopt appropriate research models for demonstration, analyze the research hypothesis through demonstration, verify the accuracy and rationality of the hypothesis, and then draw a conclusion.

3.3. Test Scheme

(1) ESG and enterprise value

H1a: ESG performance is positively correlated with enterprise value.

H1b: ESG performance is negatively correlated with enterprise value.

(2) Sample selection and data source determination

(3) Descriptive statistical analysis

(4) Draw a conclusion

4. NOVELTIES OF THE PROPOSED TOPIC

At present, most literatures mainly study the impact of one aspect of environment, social responsibility and corporate governance (E, S, G) on enterprise value, or conduct comprehensive studies with listed companies as research objects, and rarely study a single category of listed companies. The real estate industry is a complex industry in which the construction and sales process is closely related to environmental performance and social responsibility. Based on the research results, this paper will make reasonable policy suggestions for real estate enterprises from three perspectives (enterprises, governments and investors).

5. EMPIRICAL ANALYSIS

5.1. The Impact of ESG Performance on Firm Value

5.1.1. The influence mechanism of ESG performance on the book value of enterprises

Based on the comprehensive study by Wang Bo and Yang Maojia [10] regarding the mechanisms underlying the impact of ESG performance on enterprise value, it becomes evident that the fulfillment of ESG responsibilities serves as a pivotal internal force driving enterprise value creation. Excellent ESG performance serves as a testament to the resilience and sustainability of an enterprise's long-term operations, hinting at the potential for value growth. Consequently, such performance positively influences the enhancement of an enterprise's book value, underscoring the critical role of ESG in value creation and sustainability.

5.1.2. The mechanism by which ESG performance exerts its influence on the market value of a firm

Wang Bo and Yang Maojia hold the view that a favorable assessment of the fulfillment of ESG responsibilities can effectively offset the challenges posed by asymmetric information among investors. By disseminating more positive signals, it integrates responsible and sustainable ESG management practices into stock prices, thereby bolstering investor confidence and elevating the market value of enterprises. This approach underscores the significance of ESG performance in fostering trust and enhancing the overall worth of organizations.

Wang Linlin, Lian Yonghui, and Dong Jie [11] discovered that non-state-owned enterprises experience a more pronounced enhancement in enterprise value when they improve their ESG performance. Therefore, non-state-owned enterprises should prioritize the development of their ESG practices to effectively attract crucial resources from investors, consumers, governments, and other stakeholders. This approach underscores the importance of ESG in enhancing the competitiveness and long-term sustainability of non-state-owned enterprises.

5.2. The Influence of ESG Performance on the Valuation of Real Estate Enterprises

This paper will select 10 leading real estate enterprises in China, including state-owned enterprises and non-state-owned enterprises, and compare the ESG index and stock price of these 10 companies in 2020-2023.

By comparing the ESG rating of the wind database, it can be found that the ESG performance of real estate enterprises often receives more attention and supervision due to their larger scale and influence, and the relationship between the ESG index and stock price of these enterprises is more significant, especially for non-state-owned real estate enterprises.

6. SUMMARY AND SUGGESTION

At present, most large-scale listed real estate enterprises have set up a special ESG related management organization structure, such as ESG group, sustainable development committee, etc. In recent years, with the board of directors and ESG-related management organizations, large-scale housing enterprises have continuously improved the organizational framework and executive functions of ESG management and promoted the strategic goals of ESG development. The ESG report is also more comprehensive. However, from the perspective of development status, the ESG development level of the domestic real estate industry as a whole is still in the early stage. Large housing enterprises such as Country Garden, Evergrande, Vanke, Sunac, Poly, China Sea, etc., have more power and resource investment to improve the level of ESG development in all aspects under

the scale effect, while the ESG of small and medium-sized housing enterprises still has a large space for development and growth.

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