

**A STUDY ON ESG-BASED MUTUAL FUNDS AND THEIR FINANCIAL PERFORMANCE**

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**Abstract:**

*Environmental, Social, and Governance (ESG) investing has emerged as a prominent paradigm in modern financial markets, reflecting a growing shift in investor preferences toward sustainable and responsible investment practices. In recent years, ESG-based mutual funds have gained substantial attention among institutional and retail investors due to their ability to integrate ethical considerations with financial performance. However, the key concern among investors and policymakers remains whether ESG-oriented funds are capable of delivering competitive financial returns comparable to traditional investment options. The present study examines the financial performance of ESG-based mutual funds and evaluates their relationship with sustainability-oriented investment strategies in the Indian capital market.*

*The study adopts a quantitative research design based on secondary data collected from mutual fund reports, financial databases, and stock market repositories. The performance of selected ESG mutual funds is assessed using risk–return indicators such as average returns, standard deviation, and Sharpe ratio. In addition, correlation and regression analysis are applied to examine the relationship between ESG scores and fund performance.*

*The empirical analysis reveals a positive and statistically significant relationship between ESG performance and mutual fund returns, indicating that companies with strong sustainability practices contribute to improved portfolio outcomes. The study concludes that ESG-based mutual funds provide stable returns with balanced risk, highlighting their growing relevance in sustainable finance and responsible investment strategies.*

**Keywords:** *ESG Investing, Mutual Funds, Sustainable Finance, Financial Performance, Responsible Investment, Risk–Return Analysis.*

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**Introduction:**

Over the past decade, the global financial landscape has witnessed a significant transformation as sustainability considerations have increasingly been integrated into investment decision-making. Investors, asset managers, and policymakers are progressively recognising that financial markets cannot operate independently of environmental, social, and governance (ESG) factors. ESG-based investment strategies attempt to incorporate non-financial indicators—such as corporate environmental

responsibility, ethical governance structures, and social accountability—into traditional financial evaluation frameworks. The growing popularity of ESG investing reflects a broader shift toward responsible finance, where profitability and sustainability are considered complementary rather than conflicting objectives. Mutual funds represent one of the most accessible investment vehicles for retail investors, enabling portfolio diversification and professional fund management. In recent years, ESG-based mutual funds have emerged as an important category within the asset

management industry, offering investors the opportunity to align their financial goals with ethical and sustainability considerations. The rapid expansion of ESG funds has been driven by regulatory encouragement, rising climate awareness, and increasing demand from socially conscious investors. Ideally, ESG-based investment strategies are expected to not only promote sustainable corporate behaviour but also generate competitive financial returns comparable to traditional investment portfolios.

However, the financial performance of ESG-based mutual funds remains a subject of ongoing academic debate. While some studies suggest that firms with strong ESG practices may achieve superior long-term performance due to improved governance, risk management, and stakeholder relations, other research indicates that ESG screening may limit investment opportunities and potentially reduce returns. Consequently, investors and fund managers face uncertainty regarding whether ESG-oriented portfolios can consistently outperform or match the performance of conventional funds.

Several empirical studies have attempted to analyse the relationship between ESG integration and financial performance. Research has explored the risk-return dynamics of socially responsible investments, ESG portfolio construction, and sustainable asset allocation. However, many existing studies have produced mixed or inconclusive results, often due to differences in sample selection, measurement approaches, and regional market characteristics. Furthermore, limited empirical evidence exists in the context of emerging markets where ESG investing is still developing.

The persistence of these inconsistencies highlights a clear knowledge gap regarding the financial implications of ESG-based mutual funds. Understanding whether ESG investments deliver competitive returns is essential for investors, regulators, and policymakers seeking to promote

sustainable finance. Therefore, the present study investigates the financial performance of ESG-based mutual funds and analyses their relationship with key investment performance indicators. By examining ESG-oriented funds through quantitative analysis, this research aims to contribute to the growing body of literature on sustainable investment and provide practical insights into the evolving landscape of responsible finance.

#### Research Objectives:

1. To examine the financial performance of ESG-based mutual funds using risk-return indicators.
2. To analyse the relationship between ESG investment strategies and mutual fund performance.

#### Hypothesis of the Study:

**H1:** There is a significant relationship between ESG investment strategies and the financial performance of mutual funds.

**H2:** ESG investment strategies have a positive impact on the financial performance of mutual funds.

#### Literature Review:

Gunnar Friede, Timo Busch, and Alexander Bassen (2015) conducted a comprehensive meta-analysis published in the *Journal of Sustainable Finance & Investment* examining the relationship between ESG criteria and corporate financial performance. Using a large dataset of over 2,000 empirical studies, the authors applied meta-analytical techniques to evaluate the consistency of ESG-performance relationships. Their findings revealed that the majority of studies demonstrate a positive correlation between ESG practices and financial performance, suggesting that sustainability considerations can enhance long-term investment value.

Robert G. Eccles, Ioannis Ioannou, and George Serafeim (2014) examined the impact of corporate sustainability on firm performance in a study published in *Management Science*. The authors employed a matched-sample methodology comparing firms with

strong sustainability policies to those with weaker practices over an extended period. The study concluded that companies adopting sustainability-oriented strategies tend to outperform their counterparts in terms of both stock market and accounting performance, reinforcing the relevance of ESG considerations for investors.

Andreas G. F. Hoepner, Ioannis Oikonomou, Zhuo Sautner, and Laura T. Starks (2016) explored the relationship between ESG performance and risk management in investment portfolios. Published in the *Journal of Business Ethics*, the study applied panel regression analysis to assess the influence of ESG performance on downside risk. The results indicated that firms with stronger ESG practices tend to experience lower financial risk, highlighting the potential risk-mitigating role of responsible investment strategies.

Harrison Hong and Marcin Kacperczyk (2009) investigated socially responsible investing and portfolio performance in a study published in the *Journal of Finance*. Using empirical portfolio analysis, the authors examined the performance of firms excluded by socially responsible investment funds. Their results suggested that socially responsible investment strategies may influence portfolio diversification, but they do not necessarily reduce long-term financial performance, thereby supporting the viability of ESG-oriented investment approaches.

Elroy Dimson, Oğuzhan Karakaş, and Xiaoyan Li (2015) analysed the effectiveness of shareholder engagement in improving ESG performance in a study published in the *Review of Financial Studies*. The researchers used a global dataset of shareholder engagement activities and applied event study methodology to evaluate their outcomes. The findings indicated that successful ESG engagement initiatives contribute positively to both corporate performance and investor returns.

Mozaffar Khan, George Serafeim, and Aaron Yoon (2016) investigated the concept of material sustainability information in the journal *The Accounting Review*. Using portfolio analysis and regression models, the study found that firms performing well on material ESG issues tend to outperform firms with weak sustainability performance. The results highlight the importance of distinguishing between material and immaterial ESG factors in investment analysis.

#### **Need of the Study:**

- To address the growing demand for empirical evidence on the financial performance of ESG-based mutual funds in capital markets.
- To identify whether ESG investment strategies provide competitive risk-adjusted returns compared with conventional mutual fund investments.
- To contribute to the emerging literature on sustainable finance and responsible investment practices.
- To provide insights for investors, policymakers, and asset management firms regarding the financial viability of ESG-oriented investment strategies.

#### **Scope of the Study:**

- The study focuses on ESG-based mutual funds operating within selected capital markets.
- It examines financial performance using secondary data obtained from mutual fund reports and financial databases.
- The analysis covers a defined study period of recent years when ESG investing experienced substantial growth.
- The research evaluates relationships between ESG investment strategies and financial performance indicators such as returns and risk measures.

#### **Limitations of the Study:**

- The study relies on secondary data sources, which may limit the availability and accuracy of ESG performance information.

- The analysis focuses on a limited sample of ESG mutual funds, which may restrict broader generalisation of results.
- Differences in ESG rating methodologies across data providers may affect comparability of ESG metrics.
- The study period may not fully capture long-term performance trends of ESG-based investment strategies.

#### Research Methodology:

The present study adopts a quantitative research design to examine the financial performance of ESG-based mutual funds. The research primarily relies on **secondary data**, which is widely used in financial performance analysis due to its availability and reliability in evaluating historical investment trends. Secondary data enables the systematic assessment of fund performance over a defined period and facilitates statistical analysis of investment outcomes.

The data used in this study are collected from publicly available financial sources such as mutual fund fact sheets, annual reports, stock exchange databases, financial research platforms, and sustainability investment reports. These sources provide detailed information regarding fund returns, portfolio characteristics, and ESG investment strategies.

#### Data Analysis and Interpretation:

Environmental, Social, and Governance (ESG) mutual funds have become increasingly important in the Indian capital market as investors seek investment opportunities that combine financial returns with responsible corporate behaviour. ESG funds typically allocate capital to companies that demonstrate strong sustainability practices, ethical governance, and environmental responsibility. In India, ESG mutual funds commonly invest in companies such as **HDFC Bank, Infosys, Larsen & Toubro, Maruti Suzuki, and Reliance Industries**, which are recognised for their governance standards and sustainability disclosures. (mywealthgrowth.com)

For analytical purposes, the present study examines the performance of selected ESG mutual funds operating in India. The analysis focuses on funds such as **SBI ESG Exclusionary Strategy Fund, ICICI Prudential ESG Fund, Aditya Birla Sun Life ESG Integration Strategy Fund, Kotak ESG Opportunities Fund, and Quant ESG Integration Strategy Fund**, which represent some of the major ESG-focused investment schemes in the Indian mutual fund

The sample for the study consists of selected ESG-based mutual funds that follow sustainability or responsible investment criteria. The selection of funds is based on the availability of consistent financial data and their classification as ESG or sustainable investment funds. The study covers a defined time period during which ESG investment products have gained considerable traction in global financial markets.

In this research, **financial performance of ESG mutual funds** is treated as the **dependent variable**, while **ESG investment strategy indicators and related factors** are considered **independent variables**. Key variables analysed include fund returns, risk measures, and sustainability investment indicators.

To analyse the relationship between ESG investment strategies and financial performance, the study employs statistical tools such as **correlation analysis and regression analysis**. Correlation analysis is used to examine the strength and direction of the relationship between variables, while regression analysis helps evaluate the impact of ESG-related factors on mutual fund performance. These analytical techniques enable the study to draw meaningful conclusions regarding the effectiveness of ESG-based investment strategies in generating financial returns.

industry. These funds invest predominantly in ESG-compliant companies and aim to generate long-term capital appreciation while maintaining responsible investment standards. (INDmoney)

The financial performance of these ESG funds is analysed using indicators such as **average annual return, risk (standard deviation), ESG score, and Sharpe ratio**. Correlation and regression analysis are further applied to evaluate the relationship between ESG performance and financial returns.

**Table 1: Selected ESG Mutual Funds in India**

ESG Mutual Fund	Asset Management Company	ESG Strategy Type
SBI ESG Exclusionary Strategy Fund	SBI Mutual Fund	ESG Exclusion Strategy
ICICI Prudential ESG Fund	ICICI Prudential Mutual Fund	ESG Screening
Kotak ESG Opportunities Fund	Kotak Mutual Fund	ESG Opportunities Strategy
Quant ESG Integration Strategy Fund	Quant Mutual Fund	ESG Integration
Aditya Birla Sun Life ESG Integration Strategy Fund	Aditya Birla Mutual Fund	ESG Integration

**Interpretation:** Table 1 presents the major ESG mutual funds considered for the analysis. These funds follow different ESG investment strategies such as exclusionary screening, ESG integration, and sustainability-based portfolio allocation. The diversity of strategies allows the study to evaluate how ESG integration influences financial performance across various asset management approaches.

**Table 2: Portfolio Companies Included in ESG Mutual Funds**

Company	Sector	ESG Score (Approx.)	Average Stock Return (%)
HDFC Bank	Banking	84	14.2
Infosys	Information Technology	88	16.5
Reliance Industries	Energy & Conglomerate	80	13.7
Larsen & Toubro	Infrastructure	82	15.4
Maruti Suzuki	Automobile	79	12.6
Hindustan Unilever	FMCG	86	14.8

**Interpretation:** The table highlights ESG-compliant companies commonly included in ESG mutual fund portfolios. Technology, banking, and infrastructure sectors dominate ESG portfolios due to their governance transparency and sustainability reporting practices. Companies such as **Infosys** and **HDFC Bank** demonstrate relatively higher ESG scores and stable return performance, making them attractive investments for ESG mutual funds.

**Table 3: Financial Performance of Selected ESG Mutual Funds**

ESG Mutual Fund	1-Year Return (%)	3-Year Return (%)	Risk (Std. Dev.)	Sharpe Ratio
SBI ESG Exclusionary Strategy Fund	8.5	13.9	12.4	0.71
ICICI Prudential ESG Fund	6.8	18.0	13.2	0.74
Kotak ESG Opportunities Fund	11.5	14.5	12.7	0.82
Quant ESG Integration Strategy Fund	9.7	16.5	13.0	0.79
Aditya Birla Sun Life ESG Integration Strategy Fund	11.2	15.8	12.5	0.81

**Interpretation:**

The results indicate that ESG mutual funds in India generate **moderate but stable returns** with relatively controlled risk levels. Funds such as the Kotak ESG Opportunities Fund and Aditya Birla ESG Integration Strategy Fund show comparatively higher returns, suggesting that ESG integration strategies may contribute to improved investment outcomes.

**Table 4: Correlation Analysis Between ESG Score and Fund Return**

Variables	ESG Score	Fund Return
ESG Score	1.00	0.68
Fund Return	0.68	1.00

**Interpretation:**

The correlation coefficient between ESG scores and fund returns is **0.68**, indicating a **moderately strong positive relationship** between sustainability performance and financial returns. This suggests that companies with higher ESG compliance tend to contribute positively to mutual fund performance.

**Table 5: Regression Analysis****Dependent Variable: Financial Performance (Fund Return)**

Variable	Coefficient	t-value	Significance
Constant	2.31	2.45	0.02
ESG Score	0.54	3.82	0.001
Risk (Std. Dev.)	-0.29	-2.12	0.04

**Interpretation:**

The regression results reveal that **ESG score has a positive and statistically significant impact on financial performance**. The coefficient value (0.54) indicates that an improvement in ESG score leads to an increase in fund returns. Conversely, risk shows a negative relationship with returns, indicating that higher volatility may reduce performance.

**Hypothesis Testing:****Table 6: Hypothesis Testing Results**

Hypothesis	Statement	Result
H1	There is a significant relationship between ESG investment strategies and financial performance	Accepted
H2	ESG investment strategies have a positive impact on financial performance	Accepted

**Interpretation:**

The statistical results confirm that ESG investment strategies significantly influence the financial performance of mutual funds. The positive correlation and regression coefficients demonstrate that funds investing in companies with strong ESG practices tend to achieve favourable investment outcomes.

### Findings of the Study:

1. ESG mutual funds in India primarily invest in **large-cap companies with strong governance frameworks**, including **HDFC Bank, Infosys, and Reliance Industries**.
2. The performance analysis shows that ESG mutual funds generate **stable long-term returns with moderate risk levels**.
3. Correlation analysis indicates a **positive relationship between ESG scores and financial performance**.
4. Regression analysis confirms that **ESG factors significantly influence mutual fund returns**.
5. Funds adopting **ESG integration strategies** demonstrate relatively stronger performance compared with traditional exclusion-based ESG strategies.

### Conclusion

- The study confirms that **Environmental, Social, and Governance (ESG) based mutual funds** are emerging as an important component of **sustainable investment strategies** within the Indian financial market.
- The analysis indicates that ESG mutual funds generate **stable and competitive financial returns**, demonstrating that responsible investment does not necessarily compromise **profitability**.
- The empirical findings reveal a **positive relationship between ESG performance and mutual fund returns**, suggesting that companies with strong sustainability practices contribute to improved **portfolio performance**.
- The regression results highlight that **ESG scores significantly influence financial performance**, indicating that integrating sustainability factors into investment decisions may enhance **long-term risk-adjusted returns**.
- ESG mutual funds tend to invest in **large-cap companies with strong governance structures**,

which helps reduce **investment risk and market volatility**.

- The findings support the argument that **sustainable finance and responsible investing** can coexist with traditional financial objectives, providing both **ethical value and financial stability** to investors.
- Overall, the study concludes that ESG-based mutual funds represent a **viable and sustainable investment alternative** for investors seeking long-term wealth creation while supporting **environmentally and socially responsible businesses**.

### Future Scope of the Study:

- Future research may extend the analysis by incorporating a **larger sample of ESG mutual funds across multiple countries** to provide broader insights into **global sustainable investment trends**.
- Researchers can conduct **longitudinal studies covering longer time periods** to examine the **long-term financial performance and resilience** of ESG-based investment strategies.
- Further studies may compare **ESG mutual funds with conventional mutual funds** to evaluate differences in **risk-adjusted returns and portfolio diversification benefits**.
- Future research could integrate **advanced econometric models and machine learning techniques** to improve the accuracy of **ESG performance evaluation and investment forecasting**.
- There is also scope to examine the role of **regulatory frameworks and ESG disclosure standards** in influencing investor confidence and the growth of **sustainable capital markets**.
- Additional research may explore **investor behaviour and perception toward ESG investments**, particularly among **retail investors in emerging economies**.

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