

ESG and Climate Finance in Financial Economics: A Systematic Review of Recent Evidence from Leading Finance Journals

Mrityunjay K Tiwary

Finance and Accounting, Indian Institute of Management Lucknow, Uttar Pradesh, India

Abstract:

Environmental, social, and governance (ESG) considerations have become an increasingly prominent topic within financial economics over the past decade. Growing attention to climate-related financial risks, the rapid expansion of sustainable investment strategies, and the introduction of environmental disclosure regulations have collectively reshaped both academic research agendas and capital market practices. Reflecting these developments, leading finance journals have published a growing body of empirical and theoretical work examining how environmental risks and sustainability preferences influence asset prices, corporate financial policies, and financial intermediation. Despite this expansion, the literature remains dispersed across several subfields, including asset pricing, corporate finance, and banking, often employing distinct empirical approaches and conceptual frameworks.

This article provides a systematic review of recent research on ESG and climate finance published in leading finance journals. Drawing on bibliographic searches conducted through major academic databases—including Web of Science, Scopus, Google Scholar, and SSRN—the review synthesizes evidence from widely cited studies examining the financial implications of sustainability-related risks and investor preferences. The analysis organizes the literature into several major research themes: climate risk and asset pricing, institutional demand for sustainable investments, corporate sustainability and financing decisions, and the development of green financial instruments.

A growing body of empirical evidence suggests that environmental risks and investor sustainability preferences can influence financial market outcomes. For example, Hong and Kacperczyk (2009) demonstrate that firms operating in socially controversial industries—so-called “sin stocks”—exhibit higher expected returns, consistent with limited investor participation due to social norms. More recent research has extended this insight to environmental risks. Pastor, Stambaugh, and Taylor (2021) develop a theoretical asset-pricing framework in which investor preferences for sustainable firms affect equilibrium expected returns. Consistent with this perspective, Bolton and Kacperczyk (2021) document that firms with higher carbon emissions exhibit different return dynamics, suggesting that investors increasingly price exposure to carbon risk. At the same time, research on sustainable debt markets shows that the rapid growth of green bonds has created new channels for financing environmentally oriented investments; for instance, Flammer (2021) provides evidence that corporate green bond issuance is associated with increased environmental investment.

While these studies provide growing evidence that sustainability considerations are becoming embedded within financial markets, important methodological challenges remain. In particular, Berg,