



International Journal of Multidisciplinary Research in Science, Engineering and Technology

(A Monthly, Peer Reviewed, Refereed, Scholarly Indexed, Open Access Journal)



Impact Factor: 8.206

Volume 9, Issue 3, March 2026



International Journal of Multidisciplinary Research in Science, Engineering and Technology (IJMRSET)

(A Monthly, Peer Reviewed, Refereed, Scholarly Indexed, Open Access Journal)

Do ESG Scores Influence Customer Trust and Loyalty in Indian Retail Banking

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ABSTRACT: This paper will look at the impact of the perceived Environmental, Social, and Governance practices on the customer trust and loyalty to retail banking customers in India, with the customer trust as an intermediate variable. Although the literature on ESG has focused on firm-level financial performance, little focus has been put on customer-level relational performance, especially in emerging markets. The current study is grounded in the Stakeholder Theory and Commitment-Trust Theory and is based on a cross-sectional survey of 100 customers of retail banks and a path analysis of regression with 5,000 bootstrap re-samples. The customer trust is highly predicted by perceived ESG practices and customer loyalty is directly affected by the perceived ESG practices.. Customer trust is an important predictor of loyalty and partial mediation is found to exist via customer trust in the model showing 68.9 percent of the loyalty variance. The ratings of governance and social dimensions are higher than the ratings of environmental responsibility, indicating the contextual priorities of Indian retail banking customers. The results place ESG performance as a strategic relational resource that has actionable customer retention implications in banking in developing economies.

KEYWORDS: customer loyalty, customer trust, retail banking, sustainable finance, ESG practices, India.

I. INTRODUCTION

The Environmental, Social and Governance (ESG) criteria have gone far beyond their beginning in the investment analysis to influence customer perception in the service based industries. The financial impact in banking Mastering relationships based on trust, credibility, and long-term commitment ESG performance can affect customer attitudes and retention in a way that has financial implications on institutions. Retail banks operating in India are also starting to incorporate ESG into their operations and strategic management framework due to regulatory requirements, the sustainability discussion, and the growing consumer consciousness. Irrespective of this impetus, the ESG literature has focused a lot on firm-level performance - stock markets, capital cost, institutional risk - and relational outcomes at the customer-level have remained largely uncharted, especially in emerging economies.

This paper fills the aforementioned gap by exploring the research question whether perceived ESG practices are relevant to customer trust and loyalty in Indian retail banking, and whether trust mediates the ESG-loyalty relationship. The article adds to a developing literature on the customer-focused approach to ESG, offering empirical data on an underserved developing-economy setting.

II. LITERATURE REVIEW

2.1 ESG Performance and Responsible Banking.

ESG has become a paradigm of strategy with which banks express accountability, ethics and sustainability. Information asymmetry is minimised through transparency and effective governance structures (Bushman and Smith, 2001), and the Stakeholder Theory suggests that organisations that conduct themselves in a responsible manner across the stakeholder groups create legitimacy and better relational performances (Freeman et al., 2010). Higher-ESG banks are empirically found to have greater legitimacy, less reputational risk, and greater stakeholder trust (Eccles et al., 2014; Esteban-Sanchez et al., 2017).



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2.2 Customer ESG and Trust Perceptions.

Customers do not only judge banks by the quality of their services and their price, but also their ethical behaviors as well as their social contribution and transparency in their governance (Du et al., 2010; Kartsonakis and Grigoroudis, 2023). Positive judgments and emotional attachment ensue when the customers feel that there is a match between their own values and the ESG commitments of a bank. The most important thing is authenticity; performative ESG will tarnish credibility. The dimensions of governance and social aspects are likely to have more influence on customer attitudes as compared to environmental initiatives because they can be more directly experienced by retail customers (Eccles et al., 2014; Fatma and Khan, 2023). Margolis and Walsh (2003) also substantiate this: socially responsible practices are linked to organisational stability and legitimacy - ESG investments give an impression of institutional integrity, perceived financial risk among depositors and borrowers decreases.

2.3 Confidence as Intermediary between ESG and Loyalty.

Banking is built on customer trust. The Trust-Commitment Theory (Morgan and Hunt, 1994) places the trust as the key mechanism that converts the relationship inputs to the loyalty outputs. Sirdeshmukh et al. (2002) establish that trust - which refers to the confidence in the ability, goodwill and ethics of a firm to fulfill its commitments - lessens the perceived risk and increases the relational commitment which leads to loyalty. ESG information about the quality of governance and ethical management can significantly increase trust perceptions in high-information-asymmetry settings such as banking (Eisingerich and Bell, 2008; Martinez and Rodriguez del Bosque, 2013). Banks whose ESG reputations are high also enjoy a higher level of corporate image and emotional attachment which lowers switching intentions and raises advocacy (Perez and del Bosque, 2015; Mandhachitara and Poolthong, 2011; Muflih, 2021). There is still limited empirical research that incorporates the ESG-trust-loyalty chain in Indian retail banking.

III. THEORETIC FRAMEWORK AND HYPOTHESES.

This paper is a combination of Stakeholder Theory (Freeman et al., 2010) and the Commitment-Trust Theory (Morgan and Hunt, 1994). The Stakeholder Theory justifies the reason why banks invest in ESG practices - to develop legitimacy by addressing the expectations of stakeholders. The Theory of commitment-Trust elucidates the way in which such practices result in relational outcomes, where trust is the most important mechanism that decreases uncertainty and leads to commitment. Collectively, they imply a channel in which ESG practices act as institutional cues through which the customer trust is increased, which then leads to loyalty. Theoretically, a direct ESG-loyalty channel via value congruence and corporate image is also feasible. Four hypotheses follow:

H1: Perceived ESG practices positively and significantly predict customer trust.

H2: Perceived ESG practices positively and significantly predict customer loyalty.

H3: Customer trust positively and significantly predicts customer loyalty.

H4: There is mediation between perceived ESG practices and customer loyalty through customer trust.

IV. RESEARCH DESIGN AND METHODOLOGY

4.1. The research design and sample

The design was a cross-sectional, quantitative, and explanatory design. A total of 100 customers of retail banking in India were sampled using a structured self-administered questionnaire (online). It was only open to individuals with a history of six months of active banking relationship. There was a pilot test (n = 35) that was carried out before data collection; minor wording refinements were done through pilot feedback. One lastly, the responses were all complete, and there were no extreme outliers. The sample is predominantly young: 78% aged 18-25, 14% aged 26-35, with 63% male and 35% female. About half of them have undergraduate and forty two percent postgraduate education. The bank customers in the private-sector are 53 percent, public-sector 45 percent and foreign bank customers 2 percent.

4.2 Measures

Three reflective multi-item constructs were measured on a five-point Likert scale (1 = Strongly Disagree to 5 = Strongly Agree). Perceived ESG Practices (10 items) included environmental responsibility (3 items: green strategy, responsible financing, environmental risk management), social responsibility (3 items: financial inclusion, fair treatment, stakeholder balance), and the quality of governance (4 items: corporate governance, financial transparency, risk management, regulatory compliance). Customer Trust (5 items) measured financial stability beliefs, reliability, integrity, financial confidence and long-term orientation. Customer Loyalty (5 items) was the scale of relationship



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continuity, first-choice preference, recommendation, resistance to switching and cross-buying intent. Everything was based on validated CSR, trust, and relationship marketing scales.

4.3 Analytical Strategy

Path analysis was performed using Ordinary Least Squares (OLS) regression with 5,000-resample bootstrapped significance tests to obtain standardised coefficients (beta), t-statistics and 95% bias corrected confidence intervals. This is a non-parametric method which is suitable in the sample size and does not assume normality. The mediation was measured through the indirect effects method (Preacher and Hayes, 2008); mediation type (partial: 20-80%; full: >80%) was calculated as Variance Accounted For (VAF). The common method bias was evaluated with the help of Harman single-factor PCA test; VIF tests helped to determine that there was no problematic multicollinearity.

V. RESULTS

5.1 Measurement Model

Constructs all had high internal consistency reliability (Cronbachs alpha: 0.890-0.956; Composite Reliability: 0.932-0.958). AVE values were also used to confirm convergent validity, which was found to be greater than 0.50 in all constructs. The individual item loadings were between 0.860 and 0.940 with all exceeding the 0.70 mark. The support to discriminant validity was proved: all inter-construct correlations were lower than square roots of AVE values (ESG: 0.91; Trust: 0.91; Loyalty: 0.88). (see Table 1).

Construct	Items	a	CR	AVE	sqrt(AVE)	Max Inter-Corr.
Environmental Responsibility	3	0.890	0.932	0.820	0.906	--
Social Responsibility	3	0.904	0.940	0.840	0.917	--
Governance Responsibility	4	0.939	0.956	0.846	0.920	--
Customer Trust	5	0.944	0.958	0.822	0.907	0.883
Customer Loyalty	5	0.929	0.947	0.781	0.884	0.814

Table 1. Measurement Model: Reliability, Validity, and Discriminant Validity (n = 100)

5.2 Demographic Profile

The sample demographics are summarised in Table 2. The sample was young (78% of 18-25 years), which was typical of a convenience sample through student and early career networks. The percentage of males was 63 and that of females was 35. Half of them (50 percent) had undergraduate degrees and 42 percent postgraduate degrees. The majority of the customers were banked in institutions in the private sector (53%), then the public sector (45%), and the foreign banks (2%). Banking tenure was spread across 1-3 years (39%), over 5 years (35%), and 3-5 years (26%).

Demographic Variable	Category	Frequency	Percentage (%)
Age Group	18-25	78	78.0%
	26-35	14	14.0%
	36-45	6	6.0%
	46-55	2	2.0%
Gender	Male	63	63.0%
	Female	35	35.0%
	Prefer not to say	2	2.0%
Education Level	Undergraduate	50	50.0%
	Postgraduate	42	42.0%
	Doctorate	4	4.0%
	Other	4	4.0%



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Type of Bank	Private Sector	53	53.0%
	Public Sector	45	45.0%
	Foreign Bank	2	2.0%
Banking Tenure	1-3 years	39	39.0%
	3-5 years	26	26.0%
	More than 5 years	35	35.0%

Table 2. Demographic Profile of Respondents (n = 100)

5.3 Descriptive Statistics

Table 3 shows descriptive statistics at the construct level. The mean rating of Governance Responsibility was the highest (M = 3.495, SD = 1.130), then Social Responsibility (M = 3.420, SD = 1.094), and Environmental Responsibility (M = 3.150, SD = 1.096). Customer Trust achieved the highest overall mean (M = 3.580, SD = 1.116) and Customer Loyalty averaged 3.442 (SD = 0.992). The governance > social > environmental pattern indicates that Indian retail customers experience governance transparency and social inclusion in daily banking transactions more than environmental action.

Construct / Item	Mean	Std. Dev.	Min	Max
ESG: Environmental Responsibility	3.150	1.096	1.00	5.00
ESG: Social Responsibility	3.420	1.094	1.00	5.00
ESG: Governance Responsibility	3.495	1.130	1.00	5.00
ESG Overall (Q1-Q10)	3.369	1.027	1.00	5.00
Customer Trust (Q11-Q15)	3.580	1.116	1.00	5.00
Customer Loyalty (Q16-Q20)	3.442	0.992	1.00	5.00

Table 3. Descriptive Statistics - Construct Level (n = 100)

5.4 Inter-Construct Correlation Matrix

The inter construct correlation matrix is provided in Table 4. All the correlations are significant at p less than 0.001. The correlation between ESG Overall and Customer Trust (r = 0.883) and Trust and Loyalty (r = 0.814) is theoretically correct. Support of discriminant validity is because the square-root AVE of each construct is greater than the maximum inter-construct correlation.

Construct	ESG Overall	Customer Trust	Customer Loyalty
ESG Overall	1.000		
Customer Trust	0.883	1.000	
Customer Loyalty	0.795	0.814	1.000

Table 4. Inter-Construct Correlation Matrix (p < 0.001). Sqrt AVE: ESG = 0.91, Trust = 0.91, Loyalty = 0.88.

5.5 Path Analysis and Hypothesis Testing

Bootstrapped path analysis results are presented in Table 5. All four hypotheses were supported at conventional significance levels.

H	Path	Beta	t-stat	95% CI	R2	Result
H1	ESG Practices -> Customer Trust	0.959	19.045	[0.848, 1.048]	0.780	Supported ***
H2	ESG Practices -> Customer Loyalty (direct)	0.336	2.374	[0.061, 0.622]	0.689	Supported *
H3	Customer Trust -> Customer Loyalty	0.451	3.515	[0.196, 0.696]	0.689	Supported ***
H4	ESG -> Trust ->	0.433	3.380	[0.181,	--	Partial



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	Loyalty (indirect)		0.691]		mediation VAF=56.3%
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Table 5. Path Analysis and Hypothesis Testing (n = 100); *** p < 0.001 | * p < 0.05; 5,000 bootstrap re-samples

H1 was strongly confirmed: ESG practices explained 78.0% of variance in customer trust (beta = 0.959, p < 0.001). H2 was supported with a moderate direct effect (beta = 0.336, p < 0.05), confirming ESG independently influences loyalty beyond the trust channel. H3 was supported (beta = 0.451, p < 0.001), consistent with trust as a primary loyalty antecedent. H4 was confirmed: the indirect effect (beta = 0.433, 95% CI [0.181, 0.691]) excluded zero, and the VAF of 56.3% indicated partial mediation. The model explained 68.9% of variance in customer loyalty.

VI. DISCUSSION

6.1 ESG as an Institutional Trust Signal

The high ESG-trust (= 0.959) validates the argument that Indian retail banking clients engage proactively in the interpretation of ESG activities as credibility signals, which is in line with Bushman and Smith (2001) on transparency in governance and Fatma and Khan (2023) on trust driven by CSR. The greater average scores of governance (M = 3.495) and social responsibility (M = 3.420) as compared to environmental dimensions (M = 3.150) are indicative of the fact that these two dimensions are more likely to be experienced in the daily running of a bank (through regulatory compliance, ethical treatment, and financial inclusion) and as such more likely to be perceived as trust cues.

6.2 Dual ESG-Loyalty Pathways

Partial mediation (VAF = 56.3) indicates that ESG has two parallel ways of affecting loyalty. The trust-mediated channel (approximately a half of total effect) transforms ESG signals into lower risk perceptions and increasing relational commitment (Morgan and Hunt, 1994; Sirdeshmukh et al., 2002). The direct route (approximately 44%) works via value congruence and corporate image - consumers can bank with ESG-congruent banks without basing their decision on calculated trust ratings (Perez and del Bosque, 2015; Mandhachitara and Poolthong, 2011).

6.3 Theoretical and Contextual Contributions.

This paper contributes in three main ways. To begin with, it expands the scope of ESG studies based on the firm-level financial performance to the customer-level relational performance, making ESG a source of customer-related financial sustainability. Second, it confirms the Stakeholder Theory-Commitment-Trust Theory combination as a theory explaining ESG-induced customer behaviour. Third, it provides context-specific evidence in the retail banking industry in India, where governance and social aspects prove more important to customers than environmental ones - warning against extrapolation of Western market results.

VII. MANAGERIAL IMPLICATIONS

The beta = 0.959 ESG-trust coefficient indicates that the ESG engagement is not peripheral to the quality of relationships in the Indian retail banking, but rather central. Banks need to consider ESG as an investment in institutional credibility and not as a cost of compliance. The initiatives in governance transparency (ethical leadership, regulatory compliance, financial disclosure) and social responsibility (financial inclusion, fair treatment, complaint redressal) are to be prioritized in the communication as they are the most relevant to the customers. Since the ESG-loyalty relationship is achieved in both the trust-building and direct image/value channel, banks may seek to implement an integrated approach: nurturing trust through genuine and context-specific ESG reporting (not generic greenwashing-prone statements) and reputational ESG capital through products based on sustainability and community involvement. Authentic ESG distinction in the context of a commoditised competitive world provides a non-price benefit that is more substantial, especially to younger, more educated groups that constituted the majority of this sample.

VIII. LIMITATIONS AND FUTURE RESEARCH

There are a number of constraints that should be mentioned. The sample (n = 100) restricts the generalisability; the high proportion of young people (78% aged 18-25) in the sample might not be representative of the Indian population of retail banking. The cross-sectional design does not allow the causal inference across time. The single-factor test by Harman (the first factor explained 68.21 percent of the variance) suggests the possibility of common method bias in



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self-reported information. ESG is also assessed through customer perception than objective third party ratings, which bring about possible individual level variance. In the future, longitudinal designs that can be used to follow ESG-trust-loyalty dynamics through regulatory or reputational events should be utilized. Decomposition of ESG into sub-dimensions in structural models would help in explaining differential impacts. Moderating effects of bank type may be found in comparative studies on the public-sector, private-sector, and foreign banks. Theoretically inspired moderators to be examined in the future include customer characteristics: ESG awareness, age group, digital banking use.

IX. CONCLUSION

The paper presents strong evidence that customer trust and customer loyalty are strong outcomes of perceived ESG practices in Indian retail banking. ESG practices explain 78 percent of variance in customer trust and the integrated model explains 68.9 percent variance in customer loyalty. Trust-based partial mediation (VAF = 56.3) demonstrates two ESG mediating paths - trust-building and direct value alignment - both of which are important in customer retention strategy. The leading ESG drivers of Indian retail banking clients are governance and social responsibility, which highlights the significance of context-specific ESG models in emerging markets. These results rebrand ESG performance as a relational asset that is visible to the customer, and not merely an investor-facing compliance cost. To practitioners, genuine and transparent ESG practice also provides quantifiable benefits in customer retention and promotion. To researchers, this paper presents an agenda of fruitful collaboration between sustainable finance and relationship banking in less represented market environments.

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