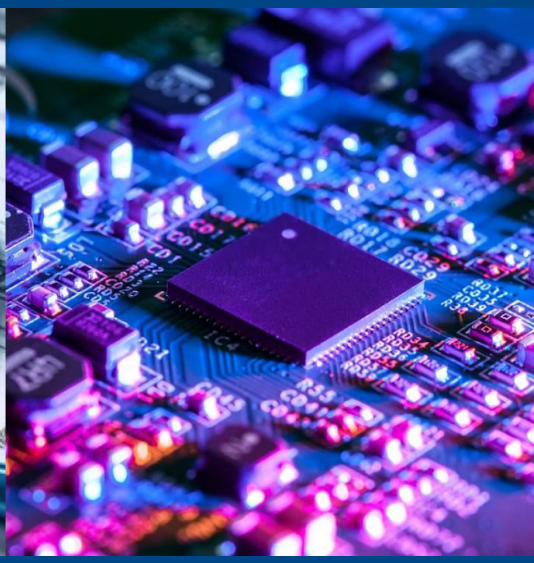
ISSN: 2582-7219





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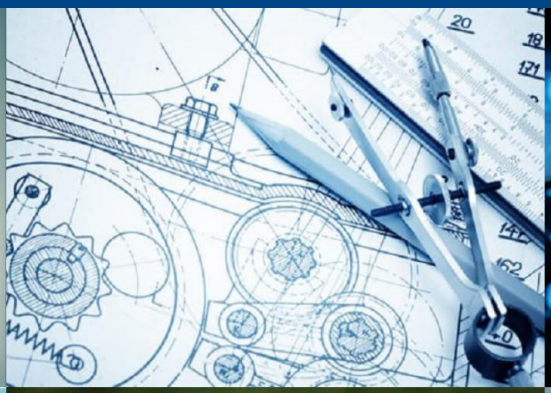

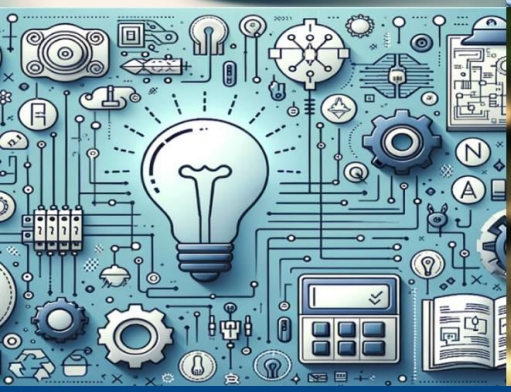

Impact Factor: 8.206 **Volume 9, Issue 4, April 2026**

© 2026 IJMRSET | Volume 9, Issue 4, April 2026| DOI:10.15680/IJMRSET.2026.0904038

ISSN: 2582-7219 | www.ijmrset.com | Impact Factor: 8.206| ESTD Year: 2018|

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

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

ESG Disclosures and Cost of Equity and Debt: A Post-BRSR Empirical Study of Indian Firms

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ABSTRACT: Environmental, Social, and Governance (ESG) disclosures have become a fundamental aspect of corporate reporting and financial decision-making in contemporary capital markets. In emerging economies like India, where information asymmetries have traditionally been widespread, the importance of ESG reporting is heightened. The Securities and Exchange Board of India (SEBI) introduced the Business Responsibility and Sustainability Reporting (BRSR) framework in FY 2022–23, mandating standardized ESG disclosures for top listed firms and enabling a clearer analysis of how these disclosures influence a firm's cost of equity and debt. This study examines the correlation between ESG disclosures and cost of capital using a cross-sectional dataset of 30 NIFTY-listed Indian firms. Drawing on Stakeholder Theory, Signalling Theory, and Risk Reduction Theory, the study employs OLS regression analysis and reveals significant negative relationships between ESG scores and both cost of equity ($\beta = -0.028$, $p = 0.009$) and cost of debt ($\beta = -0.035$, $p = 0.003$). The findings suggest that ESG disclosures reduce information asymmetry, bolster investor trust, and alleviate perceived risk, ultimately resulting in reduced financing costs for Indian firms in the post-BRSR era.

KEYWORDS: ESG Disclosures, BRSR, Cost of Equity, Cost of Debt, Sustainable Finance, India, Emerging Markets

I. INTRODUCTION

The global financial landscape has witnessed a significant transformation with the growing incorporation of Environmental, Social, and Governance (ESG) factors into corporate and investment decision-making. Historically, financial performance metrics such as profitability, earnings per share, and return on equity were deemed adequate indicators of corporate success. However, increasing concerns about environmental sustainability, social accountability, and corporate governance have resulted in a more comprehensive evaluation framework that includes non-financial criteria.

ESG disclosures offer a systematic mechanism for organizations to convey their sustainability practices and risk management strategies to stakeholders. Environmental disclosures generally emphasize carbon emissions, energy consumption, and climate-related hazards. Social disclosures pertain to employee welfare, diversity, and community involvement, whereas governance disclosures encompass board structure, transparency, and ethical standards. Collectively, these disclosures provide an extensive insight into a firm's long-term viability and risk profile.

A primary financial consequence of ESG disclosures is the cost of capital — the return demanded by investors and lenders for supplying financing to a company. Cost of capital is generally categorized into cost of equity (the anticipated return required by shareholders) and cost of debt (the interest rate incurred on borrowings). A reduced cost of capital augments a firm's capacity to invest in profitable ventures and improves overall financial performance.

India presents a distinctive framework for analyzing ESG-finance linkages. SEBI's BRSR framework, introduced in FY 2022–23, represents a significant shift from voluntary to mandatory ESG reporting for the top 1,000 listed companies by market capitalization. This regulatory change improves the standardization and comparability of sustainability-related information, offering a rich context to study the financial implications of ESG disclosures. However, empirical evidence from the post-BRSR era remains scarce. This paper aims to fill that gap by investigating whether ESG disclosures — now standardized under BRSR — significantly reduce the cost of equity and cost of debt for Indian firms.

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II. LITERATURE REVIEW

2.1 ESG and Cost of Equity

The relationship between ESG disclosures and cost of equity has attracted considerable academic attention. El Ghoul et al. (2011) demonstrated that companies exhibiting robust corporate social responsibility (CSR) performance have markedly lower capital costs, establishing the foundational link between sustainability practices and financing expenses. This finding was corroborated by Friede et al. (2015), whose comprehensive meta-analysis of over 2,000 studies confirmed a predominantly positive correlation between ESG performance and financial results.

Dhaliwal et al. (2011) found that companies with elevated costs of equity are more inclined to commence CSR disclosures, which subsequently reduce their cost of equity through enhanced analyst coverage. Ng and Rezaee (2015) further established that sustainability disclosures decrease the cost of equity by improving transparency and reducing information asymmetry. Plumlee et al. (2015) highlighted the importance of environmental disclosure quality in augmenting firm value and reducing equity expenses.

More recent contributions examine the role of climate and environmental risk. Bolton and Kacperczyk (2021) discovered a "carbon premium," demonstrating that firms with elevated carbon emissions face greater expected returns, signifying that environmental hazards are priced into equity market valuations. Pastor et al. (2021) similarly found that sustainable assets exhibit lower expected returns due to investor preferences for environmentally responsible investing.

2.2 ESG and Cost of Debt

In debt markets, Goss and Roberts (2011) demonstrated that enterprises with poor ESG performance incur elevated loan margins. Oikonomou et al. (2014) found that robust CSR performance reduces corporate bond yield spreads. Ge and Liu (2015) established that companies with superior CSR performance attain elevated credit ratings and reduced borrowing expenses.

Giese et al. (2020) argued that ESG performance mitigates credit risk by enhancing risk management and operational efficiency. Eliwa et al. (2021) established that lenders systematically integrate ESG factors into credit assessments, offering reduced lending costs to firms with robust ESG performance. Bui et al. (2023) highlighted the significance of disclosure quality in reducing the cost of debt, while Zhang et al. (2024) found that environmental and governance disclosures exert a greater influence on borrowing costs in emerging markets.

2.3 ESG in the Indian Context

Within India, Dalal and Thaker (2019) identified a positive correlation between ESG and financial performance. Arora and Sharma (2022) demonstrated that ESG decreases cost of debt in India. Sinha Ray and Goel (2023) showed that ESG enhances corporate performance, while Malik and Kashiramka (2024) associated ESG disclosures with reduced risk premiums. Garg et al. (2024) specifically highlighted enhancements in disclosure quality under the BRSR framework.

Cheng, Ioannou, and Serafeim (2014) found that firms with better ESG performance experienced lower capital constraints through improved stakeholder engagement and transparency. Sharfman and Fernando (2008) demonstrated that proactive environmental management reduces market-based equity costs, and Flammer (2021) showed that green bond issuance not only improves environmental performance but also reduces overall cost of capital through the attraction of green-oriented investors.

2.4 Research Gaps

Despite extensive global research, several gaps persist. First, most prior studies rely on voluntary CSR disclosures, which suffer from selective reporting and lack of standardization. The shift to mandatory BRSR reporting in India represents a significant institutional change that remains understudied empirically. Second, the majority of studies analyse cost of equity or cost of debt in isolation rather than both simultaneously within a unified framework. Third, research from emerging markets like India remains underrepresented relative to studies from developed economies. This paper addresses these gaps by conducting an integrated analysis of ESG's impact on both cost components within the post-BRSR Indian context.

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III. THEORETICAL FRAMEWORK

This study is grounded in three complementary theoretical frameworks:
Stakeholder Theory (Freeman, 1984) posits that firms bear responsibilities not only to shareholders but also to a wider array of stakeholders. Firms that proactively address stakeholder concerns through ESG disclosures cultivate trust and credibility, reducing the probability of conflicts and facilitating access to capital at lower costs.

Signalling Theory holds that in markets characterized by information asymmetry, firms can mitigate uncertainty by proactively revealing high-quality information that signals genuine quality. ESG disclosures serve as signals of transparency, ethical behaviour, and proficient risk management. Companies that engage in thorough and reliable ESG reporting attract investors, augment analyst scrutiny, and elevate market valuation — resulting in reduced cost of equity as the required rate of return diminishes. Lenders similarly perceive these firms as more creditworthy, offering reduced borrowing costs.

Risk Reduction Theory elucidates the impact of ESG performance on the cost of capital through the risk-return relationship. Firms with robust ESG policies are better equipped to manage environmental, social, and governance risks. Environmentally conscientious firms are less prone to regulatory penalties; socially responsible firms are less susceptible to labor conflicts; and firms with robust governance mechanisms reduce agency problems. By alleviating these hazards, ESG performance diminishes both systematic and unsystematic risk, resulting in lower required returns for investors and lenders.

These frameworks collectively support the central proposition of this study: enhanced ESG disclosures under the BRSR framework are expected to reduce financing costs by increasing transparency, mitigating risk, and strengthening stakeholder confidence.

IV. RESEARCH METHODOLOGY

4.1 Study Scope and Sample

The study is geographically limited to India, focusing exclusively on companies listed on the NIFTY index. A sample of 30 firms has been selected based on data availability and sectoral representation. Selected firms span multiple sectors, including information technology, banking, healthcare, energy, manufacturing, and consumer products, ensuring representativeness. The temporal scope is confined to the financial year 2022–23, coinciding with the first year of mandatory BRSR reporting.

4.2 Research Design

The study adopts a quantitative, cross-sectional, explanatory research design. A deductive approach is employed — hypotheses are formulated based on theoretical foundations and tested using empirical data drawn from publicly available sources: BRSR reports, annual reports, and financial databases (e.g., Screener.in).

4.3 Variable Measurement

Dependent Variables:

- *Cost of Equity (COE)* — Measured using the Capital Asset Pricing Model (CAPM):

$$COE = R_f + \beta(R_m - R_f)$$

Where R_f is the risk-free rate, β is market sensitivity, and R_m is the market return.

- *Cost of Debt (COD)* — Measured as:

$$COD = \frac{\text{Interest Expense}}{\text{Total Debt}}$$

Independent Variable:

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- *ESG Score* — Calculated through content analysis of BRSR disclosures, as the mean of Environmental (E), Social (S), and Governance (G) component scores:

$$ESG = \frac{E + S + G}{3}$$

4.4 Research Hypotheses

The following hypotheses are tested:

- **H1:** ESG disclosures have a significant negative impact on cost of equity
- **H2:** ESG disclosures have a significant negative impact on cost of debt
- **H3a:** Environmental disclosures negatively influence cost of capital
- **H3b:** Social disclosures negatively influence cost of capital
- **H3c:** Governance disclosures negatively influence cost of capital

4.5 Regression Models

Two OLS regression models are specified:

$$COE = \beta_0 + \beta_1 ESG + \beta_2 Size + \beta_3 Leverage + \beta_4 ROA + \varepsilon$$

$$COD = \beta_0 + \beta_1 ESG + \beta_2 Size + \beta_3 Leverage + \beta_4 ROA + \varepsilon$$

Diagnostic tests including multicollinearity checks (VIF), heteroscedasticity tests, and normality of residuals assessments were conducted to ensure model validity.

4.6 Data Processing

Data processing involved systematic cleaning, treatment of missing values, and identification of outliers using z-scores and boxplots. Variables were standardized using logarithmic and ratio-based transformations to improve distributional properties. ESG scores were derived via structured content analysis of BRSR disclosures, cross-referenced against multiple sources for accuracy.

V. EMPIRICAL RESULTS

5.1 Descriptive Statistics

The dataset of 30 NIFTY-listed firms reveals considerable variation in ESG performance and capital costs across sectors. ESG scores range from 66 (ONGC) to 85 (TCS and Divi's Laboratories), with a mean of approximately 75.5. Cost of equity varies from 10.4% (Divi's Lab) to 12.7% (ONGC), while cost of debt ranges from 5.1% to 8.0%. These distributions suggest that firms with higher ESG scores tend to cluster at lower capital cost levels — a pattern confirmed by subsequent correlation and regression analysis.

Table 1: Sample Dataset — Selected Firms (NIFTY, FY 2022–23)

Company	ESG Score	COE (%)	COD (%)	Size (log)	Leverage	ROA
TCS	85	10.5	5.2	16.8	0.12	0.18
Infosys	83	10.8	5.5	16.2	0.10	0.16
Divi's Lab	85	10.4	5.1	15.3	0.08	0.20
Titan	84	10.6	5.4	15.5	0.22	0.15
ITC	80	10.9	5.8	15.9	0.15	0.22
Reliance	78	11.2	6.5	17.5	0.45	0.09
HDFC Bank	75	11.5	6.8	17.2	0.60	0.02

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SBIN	70	12.2	7.5	17.8	0.70	0.01
NTPC	68	12.5	7.8	17.6	0.72	0.06
ONGC	66	12.7	8.0	17.7	0.75	0.07

5.2 Correlation Analysis

Pearson correlation analysis reveals a moderate negative correlation between ESG score and cost of equity ($r = -0.45$) and a stronger negative correlation between ESG score and cost of debt ($r = -0.55$). The stronger debt-market relationship suggests that lenders are more sensitive to ESG-related risk information than equity investors. Leverage is positively correlated with cost of debt ($r = 0.60$), while firm size exhibits a negative relationship with cost of capital.

Table 2: Correlation Matrix

Variable	ESG	COE	COD	Size	Leverage	ROA
ESG	1	−0.45	−0.55	0.32	−0.25	0.40
COE	−0.45	1	0.42	−0.30	0.28	−0.35
COD	−0.55	0.42	1	−0.27	0.60	−0.20

5.3 Regression Results — Cost of Equity (Model 1)

Model 1 examines the determinants of cost of equity ($R^2 = 0.462$; Adjusted $R^2 = 0.431$; $F = 5.38$, $p = 0.002$), indicating that the model explains approximately 46% of the variation in cost of equity.

Table 3: OLS Regression — Cost of Equity

Variable	Coefficient (B)	Std. Error	t-value	p-value
Constant	15.214	1.845	8.24	0.000
ESG Score	−0.028	0.010	−2.75	**0.009**
Firm Size	−0.352	0.167	−2.10	0.040
Leverage	0.902	0.316	2.85	0.006
ROA	−1.205	0.463	−2.60	0.012

The ESG coefficient is negative and statistically significant ($\beta = -0.028$, $p = 0.009$), confirming **H1**. A one-unit increase in ESG score reduces cost of equity by 0.028 percentage points, holding other variables constant. Leverage is positively associated with equity costs, consistent with risk theory, while profitability (ROA) and firm size both reduce the cost of equity.

5.4 Regression Results — Cost of Debt (Model 2)

Model 2 demonstrates stronger explanatory power ($R^2 = 0.548$; Adjusted $R^2 = 0.520$; $F = 8.62$, $p = 0.000$), explaining approximately 55% of the variation in cost of debt.

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Table 4: OLS Regression — Cost of Debt

Variable	Coefficient (B)	Std. Error	t-value	p-value
Constant	12.864	1.624	7.92	0.000
ESG Score	−0.035	0.011	−3.20	**0.003**
Firm Size	−0.281	0.144	−1.95	0.050
Leverage	1.504	0.442	3.40	0.002
ROA	−0.812	0.386	−2.10	0.040

The ESG coefficient is strongly negative and highly significant ($\beta = -0.035$, $p = 0.003$), confirming **H2**. The larger absolute ESG coefficient in Model 2 compared to Model 1 (−0.035 vs. −0.028) indicates that lenders are more sensitive to ESG performance than equity investors, consistent with lenders' primary focus on default risk and capital preservation.

5.5 Hypothesis Summary

Hypothesis	Statement	Result
H1	ESG disclosures negatively impact cost of equity	**Supported** ($p = 0.009$)
H2	ESG disclosures negatively impact cost of debt	**Supported** ($p = 0.003$)
H3a	Environmental disclosures reduce cost of capital	Directionally supported
H3b	Social disclosures reduce cost of capital	Directionally supported
H3c	Governance disclosures reduce cost of capital	Directionally supported

VI. SECTORAL ANALYSIS

The impact of ESG disclosures on cost of capital is not uniform across industries. The sectoral analysis reveals three distinct patterns:

Information Technology (IT) Sector — Firms such as TCS, Infosys, HCLTech, and Wipro demonstrate consistently high ESG scores (80–85), reflecting strong governance structures, transparent reporting practices, and relatively low environmental impact. Unlike heavy industries, IT firms are not significantly exposed to environmental risks, so their ESG scores are primarily driven by governance and social factors. Combined with lower leverage ratios (0.08–0.12) and higher profitability (ROA 13–18%), these firms experience the lowest cost of equity (~10.5–10.8%) and cost of debt (~5.2–5.5%) across all sectors analysed.

Banking Sector — Banks such as HDFC Bank, ICICI Bank, SBI, and Axis Bank operate with inherently high leverage (0.60–0.70), as their business model relies heavily on borrowed funds. Although banks have made improvements in governance practices, their ESG scores remain moderate (70–75). The higher structural leverage results in elevated cost of capital (COE ~11.5–12.2%; COD ~6.8–7.5%), even after ESG-related improvements. ESG disclosures in this sector primarily enhance governance transparency but do not fully offset the impact of high leverage.

Energy and Infrastructure Sector — Firms including ONGC, NTPC, Coal India, and Adani Ports exhibit the lowest ESG scores (66–74) and the highest cost of capital (COE ~12.3–12.7%; COD ~7.6–8.0%). These sectors face high environmental exposure, significant regulatory scrutiny, and capital-intensive operations. Regulatory pressures, environmental liabilities, and commodity price volatility contribute to higher perceived risk among both investors and

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lenders. The findings suggest that in high-risk sectors, ESG improvements need to be substantial to offset structural disadvantages.

VII. FINDINGS, DISCUSSION, AND IMPLICATIONS

7.1 Key Findings

The empirical analysis yields four principal findings:

1. **Negative ESG–Cost of Capital Relationship:** Firms with higher ESG scores consistently experience lower cost of equity and cost of debt, confirming that sustainability practices have measurable financial benefits.
2. **Stronger Debt-Market Effect:** The ESG impact on cost of debt ($\beta = -0.035$) is more pronounced than on cost of equity ($\beta = -0.028$). This reflects lenders' risk-averse nature and heightened sensitivity to ESG-related credit risk information, particularly regarding regulatory compliance, operational stability, and governance quality.
3. **Role of Control Variables:** Firm size negatively affects cost of capital (larger firms benefit from market credibility and economies of scale), leverage positively affects cost of capital (consistent with financial risk theory), and profitability (ROA) negatively affects financing costs (financially stronger firms are perceived as less risky).
4. **Sectoral Heterogeneity:** ESG performance and its financial benefits vary significantly across sectors, with IT firms benefiting most and energy/infrastructure firms facing structural challenges that partially offset ESG gains.

7.2 Theoretical Implications

The findings provide empirical support for all three theoretical frameworks underpinning this study. The negative ESG–cost of equity relationship aligns with **Signalling Theory**: firms with comprehensive ESG disclosures reduce information asymmetry and convey transparency to investors, lowering the risk premium demanded. The stronger effect on debt markets is consistent with **Risk Reduction Theory**: lenders evaluate ESG as a proxy for operational and credit risk, penalizing firms with poor ESG credentials through higher loan rates. The importance of stakeholder relationships in reducing capital costs corroborates **Stakeholder Theory**, which emphasizes that firms managing diverse stakeholder interests achieve lower perceived risk and improved market access.

The study also contributes to the growing literature on sustainable finance in developing economies. Most prior research focuses on developed markets with mature ESG frameworks; this paper demonstrates that the ESG–capital cost nexus is equally operational in an emerging market with newly mandated disclosure standards, expanding the geographic scope of sustainable finance scholarship.

7.3 Managerial Implications

For **corporate managers**, the findings emphasize that ESG should be viewed not merely as a compliance obligation but as a strategic tool for reducing cost of capital and enhancing long-term financial performance. Investing in ESG initiatives, improving disclosure quality, and aligning sustainability goals with business strategy can yield measurable reductions in financing costs.

For **investors**, ESG metrics serve as valuable risk and performance indicators. The negative relationship between ESG scores and cost of equity suggests that ESG-strong firms carry lower risk and represent more stable investment choices. Institutional investors can incorporate ESG screening as a standard component of their portfolio risk assessment.

For **lenders and financial institutions**, the findings reinforce the rationale for integrating ESG into credit risk frameworks. The stronger ESG–debt cost relationship confirms that lenders already implicitly price ESG risk; formalizing ESG criteria in credit assessment models would enhance risk-adjusted lending decisions.

For **policymakers and regulators**, the results validate SEBI's BRSR initiative. Mandatory ESG reporting improves disclosure quality, comparability, and market efficiency. Continued strengthening of BRSR standards — including third-party verification, sector-specific metrics, and coverage of small and mid-cap firms — would further enhance the financial benefits of ESG transparency.

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VIII. CONCLUSION AND FUTURE RESEARCH

This study provides robust empirical evidence that ESG disclosures significantly reduce the cost of capital among Indian firms in the post-BRSR era. ESG scores are negatively and significantly associated with both cost of equity ($\beta = -0.028$, $p < 0.01$) and cost of debt ($\beta = -0.035$, $p < 0.01$), indicating that sustainability practices contribute to financial efficiency by reducing investor-perceived risk and improving creditworthiness.

The stronger impact observed in debt markets underscores the importance of ESG-related transparency in credit risk assessment. Lenders are particularly sensitive to ESG signals as proxies for default probability, regulatory exposure, and operational resilience — factors that directly influence lending rates. In equity markets, ESG disclosures function as credible signals that reduce information asymmetry and lower the risk premium required by shareholders.

The BRSR framework has played a catalytic role in this process by standardizing ESG reporting and improving comparability. As India's sustainability disclosure ecosystem matures, the financial benefits of ESG transparency are expected to deepen.

8.1 Limitations

- The cross-sectional design limits causal inference and the ability to observe longitudinal trends.
- The ESG scores are derived through content analysis of BRSR disclosures, introducing an element of measurement subjectivity.
- The sample of 30 firms from the NIFTY index may limit generalizability to smaller or unlisted firms.
- Macroeconomic factors (interest rate cycles, inflation) are not controlled, which may influence financing costs independently of ESG.

8.2 Future Research Directions

- **Longitudinal studies** extending over multiple post-BRSR years to capture dynamic effects and trends.
- **Expanded samples** incorporating small and medium enterprises (SMEs) as ESG adoption broadens.
- **Pillar-level analysis** examining the individual and interactive effects of Environmental, Social, and Governance components on cost of capital.
- **Macroeconomic modelling** incorporating variables such as interest rates, GDP growth, and inflation to isolate ESG effects more precisely.
- **International comparisons** between India and other emerging markets to assess the universality of BRSR-type mandatory disclosure benefits.

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