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Environmental, social and governance (ESG) performance in the context of multinational business research

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Abstract

Purpose – This paper aims to examine the state of research on environmental, social and governance (ESG) performance in the context of multinational business research. This paper discusses research progress as well as various issues and complexities associated with using ESG ratings in cross-country studies and for assessing the performance of multinational enterprises (MNE) and emerging market multinationals (EMNEs).

Design/methodology/approach – The paper identifies emerging literature that focuses on tracking the development and uptake of ESG ratings in the international context. It discusses three emerging research streams: Research examining the ESG-financial performance relationship in emerging markets, research tracking the ESG performance of multinationals in the various countries and regions they are operating, and frameworks for assessing ESG-related risks on a country level.

Findings – While the emerging body of work adds an important dimension to the identification and awareness of ESG issues globally, numerous unresolved issues become evident. ESG frameworks have been built to assess corporate sustainability as it relates to firms in their "home" countries (typically with a focus on developed countries), with limited applicability and transferability to emerging markets. International firm activities are often not captured in detail and not comprehensively mapped across firm subsidiaries and a firm's corporate supply chain where ESG issues are prone to happen, and ESG scores do not comprehensively integrate views and voices from various local stakeholders that are impacted by firm activities, particularly indigenous communities.

Research limitations/implications – Research on ESG ratings in the context of multinational business research is generally sparse and fragmented, thus creating opportunities for future research to expand on existing and emerging findings.

Practical implications – The paper creates awareness of issues to consider when using ESG ratings in cross-country studies and for assessing the ESG performance of MNEs and EMNEs: ESG scores can be subject to bias and are not weighted by materiality, which can be misleading for portfolio construction and performance measurement purposes. Managers need to be aware that ESG scores are often not capturing ESG issues occurring in supply chains and ESG issues affecting local communities.

Originality/value – This study enriches the understanding of ESG in the context of multinational business research practice.

Keywords Environmental, social and governance (ESG), Performance, Multinational enterprise (MNE)

Paper type Conceptual paper

Introduction

A substantial body of literature has developed to monitor firms' environmental, social and governance (ESG) performance. ESG ratings typically form the basis for socially responsible

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investment (SRI) strategies, a (loosely defined) umbrella term for investment practices that target firms with "positive" social and environmental profiles (Renneboog *et al.*, 2008). The rapid uptake of SRI investments has been seen as a sign that investors are not solely concerned about the financial performance of their investment portfolio but also about the social and/or environmental attributes of their investment choices (Bollen, 2007). Possible reasons might include the alignment of investments with personal values and societal expectations (Bollen, 2007), and the desire to avoid possible exposure to higher risk (van Duuren *et al.*, 2016). The rapidly growing area of SRI sparked a substantial scholarly debate regarding whether higher ESG-related performance can generate value for stakeholders – and whether instrumental stakeholder theory (which views stakeholder satisfaction as instrumental for firm financial performance) is a valid theory in the ESG context (Orlitzky *et al.*, 2003). While recent meta-analyses in the field point to generally positive associations between some aspects of ESG and financial performance (Whelan *et al.*, 2020), this finding is not universal across studies and has not been consistently replicated in developing country contexts. Discrepancies among studies have been attributed to the use of different ESG definitions and metrics (Eccles and Stroehle, 2018; Whelan *et al.*, 2020). However, discrepancies might also result from testing the ESG-financial performance (ESG-FP) relationship in different markets and regions that are characterized not only by different institutional regimes and ESG disclosure requirements but also by differences in culture, human capital as well as social and governance structure, which are often not fully captured by existing theory (Ortas *et al.*, 2019).

Given the popularity of ESG investing in developed countries with mature markets, ESG has been described as a "rich world phenomenon" (Chung, 2021). Indeed, companies in emerging markets have not been the top choice for ESG-focused investors, for several reasons. Investments in emerging markets are often seen as riskier investments due to weaker formal institutions, less stringent regulatory environments, lower protection of shareholder rights, lower levels of transparency and more widespread corruption (Bahadori *et al.*, 2021; Hoang, 2018). Firms operating in emerging markets also face challenges due to volatile governmental policy, thus creating challenges that affect the E, S and G dimensions (Bahadori *et al.*, 2021). In addition, emerging markets present additional challenges due to limited information access and an opaque information environment, meaning that reliable information on corporate ESG performance is often not readily available and easily accessible (Mobius and Ali, 2021). Nonetheless, there is now also growing recognition that typically understudied economies in Asia, Africa, Eastern Europe, the Middle East and Latin America have a substantial impact on global sustainability (Ortas *et al.*, 2019). Opportunities to tap into emerging market niches and contribute to addressing growing concerns about environmental and social issues globally are increasingly prompting investors (and researchers alike) to explore SRI investments in less mature markets, accepting potentially higher risks for higher return prospects. However, the empirical evidence on the ESG–FP relationship (also for emerging markets) is largely based on evidence and frameworks developed for the US and European/UK markets, which leads to questions about whether it is viable (and appropriate) to "export" ESG frameworks to assess ESG performance outside of Western markets [1].

Initially, literature started to trace the development and uptake of ESG in the international context, focusing on ESG disclosure practices by firms in developed versus developing markets (Chapple and Moon, 2005; Fekrat *et al.*, 1996; Gamble *et al.*, 1996; Maignan and Ralston, 2002). Studies primarily relied on theorizing the uptake of ESG as a strategic response (achievement of legitimacy, compliance and/or competitive advantages) in response to increasing institutional pressures in different countries or markets, explained by different stages of development (Chapple and Moon, 2005). The increased availability of ESG data by ESG rating providers has allowed researchers to also empirically measure ESG performance in cross-country studies (Ioannou and Serafeim, 2012). Building on these foundations, a first body of emerging work studies ESG-FP relationships for firms in emerging market settings (Duque-Grisales and Aguilera-Caracuel, 2021). Other emerging work in the field tracks the ESG performance of multinational enterprises (MNEs) in the various countries and regions in which they operate (Salsbery, 2021), primarily based on concerns about MNEs engaging in corporate social irresponsibility (CSI) in jurisdictions with less stringent formal and social institutional pressures (Brammer *et al.*, 2021). There have been additional attempts to develop frameworks for assessing ESG-related risks on a country level to assess ESG risks related to governments or government-related issuers beyond individual companies (Pollard *et al.*, 2018).

This article surveys the emerging body of work but also points to numerous unresolved issues. Specifically, the article is structured as follows: First, the background section provides an overview of research on ESG ratings in multinational business research. The following sections then offer an overview of emerging research areas and current research progress but also offer a critical discussion of current approaches, issues and complexities. These include:

- ESG frameworks have been built to assess corporate sustainability as it relates to firms in their "home" countries (typically with a focus on developed countries), but might have limited applicability and transferability study ESG in emerging markets;
- ESG scores do factor in international firm activities (e.g. Human Rights and Child Labour Policies), but these are often not captured in detail and not comprehensively mapped across firm subsidiaries and a firm's corporate supply chain (where ESG issues are prone to happen); and
- ESG scores do not integrate views and voices from various local stakeholders that are impacted by firm activities, especially Indigenous communities (Pelosi and Adamson, 2016).

Examining these issues, the article then highlights areas in which future research is needed and concludes by offering a discussion and points for future research.

Background: environmental, social and governance ratings in the international context

From the 1990s onwards, researchers started to examine the disclosure of non-financial information in corporate reports or on corporate websites in international settings (Chapple and Moon, 2005; Fekrat *et al.*, 1996; Gamble *et al.*, 1996; Maignan and Ralston, 2002). Research in this field was typically based on institutional and/or legitimacy theories to explain how differences in institutional or regulatory conditions or social acceptance lead to international variations in disclosure practices (Baldini *et al.*, 2018 as well as Ortas *et al.*, 2019 for further detailed reviews of these theoretical perspectives used to explain variation in ESG disclosure). As ESG ratings by rating agencies and data vendors became more sophisticated and commonplace, researchers began to use these data sets for the analysis of what was referred to as corporate social performance (CSP) or ESG performance. A study that is frequently cited is the analysis by Ioannou and Serafeim (2012) who obtained ESG data from Thomson Reuters ASSET4 (now Refinitiv), alongside stock market data and national-level variables, for a sample of 12,764 firm-year observations from 42 countries over seven years to analyse why firms embedded in various national-level institutions exhibit significantly different corporate social performances, concluding that variations in non-financial disclosures across countries can be attributed to institutional, political and cultural factors.

Subsequent studies used various institutional and neo-institutional lenses to address international variations in ESG disclosure. However; literature focusing on a truly international perspective of ESG activity and ESG performance is still limited – not just due to a lack of theory offering insights beyond Western paradigms, but also because of the limited availability of ESG data for firms outside of North America or Europe and resulting analytical challenges (Arun *et al.*, 2021; Orsato *et al.*, 2015; Rajesh and Rajendra, 2020). For example, even though the study by Ioannou and Serafeim (2012) included data from 42 countries, the sample was heavily focused on firms from the USA, Japan and the UK with most observations. Countries such as Chile, Indonesia, Thailand and the Philippines were represented with 5 or fewer observations in the sample. The availability of ESG data has certainly improved considerably since: A more recent study by Bhaskaran *et al.* (2020) was based on ESG data for 1,317 emerging market firms and 3,569 developed market firms. However, most observations in this study were still based on data from the US, UK and other developed markets. Similar findings apply to almost all studies drawing upon international ESG panel data, irrespective of the ESG data used (Pollard *et al.*, 2018). Finer-grained analyses of ESG performance in developing countries that consider the local environments in which a firm operates, distinguish between "cosmetic" and substantive ESG issues and recognize different levels of data quality are still largely missing (Mobius and Ali, 2021).

The limited availability of ESG ratings outside of developed markets has been driven by several factors: First, and as demonstrated by Eccles and Stroehle (2018), the origins of ESG metrics and ESG rating organizations can be traced back to the 1970s, when stakeholders including NGOs demanded information about corporate involvement in controversial issues such as nuclear weapons development or South Africa's apartheid regime. The authors traced the history of nine ESG data and analytics organizations, all with origins in the USA, UK and Europe, and show how these organizations evolved from a focus on providing information of relevance to investors and stakeholders, to eventually becoming ESG rating providers (which included several mergers and acquisitions amongst rating organizations). Second, several other institutional constraints have limited the uptake of ESG ratings globally. These include limited investor interest in nascent and shallow capital markets, limited disclosure requirements (and thus also limited data availability), as well as weak institutions, and corporate ownership structures which lead to poor disclosure outcomes (Odell and Ali, 2016; Orsato *et al.*, 2015). However, at the same time, there is recognition that it is precisely those factors that also warrant a greater focus on ESG in emerging and frontier markets (Odell and Ali, 2016).

In recent years, the ESG agenda has been accelerated by initiatives such as the adoption of the United Nations Principles of Responsible Investment (UNPRI) and the United Nations' Sustainable Development Goals (SDGs), all well as the proliferation of internationally recognized accounting frameworks such as the Global Reporting Initiative (GRI) which also provide guidelines for companies to report on ESG performance (Arun *et al.*, 2021). In addition, many countries have introduced ESG disclosure requirements – for instance, all ASEAN-6 countries (Singapore, Malaysia, Thailand, Vietnam, Indonesia and the Philippines) now require sustainability reports or disclosures for listed companies (Pan, 2021). The creation of emerging market indices (e.g. the FTSE Emerging Index) and related ETFs provide investors with new opportunities. These developments have led to several implications: First, ESG ratings providers have faced pressures to increase their ESG ratings universe to inform investors of ESG risks related to emerging market opportunities. Second, the literature has started to move beyond merely documenting differences in ESG disclosure practices due to differences in country-level environments and has instead started to analyze the implications of ESG for firms, investors, and markets (see following sections). Work has specifically focused on exploring three areas studies that investigate the ESG-FP relationship for emerging markets, studies that track the ESG performance of multinational companies (MNEs) in the various countries and studies that have started to engage with ESG-related risks on a country level (see Figure 1 for a summary). These streams are reviewed in further detail below.

The environmental, social and governance–financial performance relationship

A first emerging body of work studies ESG–FP relationships for firms in emerging market settings. Within this body of work, there is a substantially new focus on documenting the ESG-FP relationship for previously understudied settings, including Latin America (Duque-Grisales and Aguilera-Caracuel, 2021), Asia (Lee *et al.*, 2016; Ng *et al.*, 2020; Yoon *et al.*, 2018), the Middle East and North Africa (Al-Hiyari and Kolsi, 2021) and the so-called BRICS countries (Brazil, Russia, India, China and South Africa) more broadly (Ali *et al.*, 2021; Garcia *et al.*, 2017; Koroleva *et al.*, 2020; Miralles-Quirós *et al.*, 2018; Rajesh, 2020). Of these countries, China continues to receive significant research attention (Deng and Cheng, 2019; Weber, 2014, 2017; Zhang *et al.*, 2021; Zhao *et al.*, 2018), which has been driven by the opening of its financial markets to foreign investors and the introduction of more stringent environmental policies, including recent commitments towards carbon neutrality in 2060. Recent data show that over 1,000 Chinese A-share companies (i.e. companies listed on the Shanghai and Shenzhen exchanges) had published annual ESG reports, up from just 371 companies in 2009. Of these companies, about 130 have dual listings in Hong Kong, where ESG reports are mandatory (World Economic Forum, 2021). Studies have also examined the

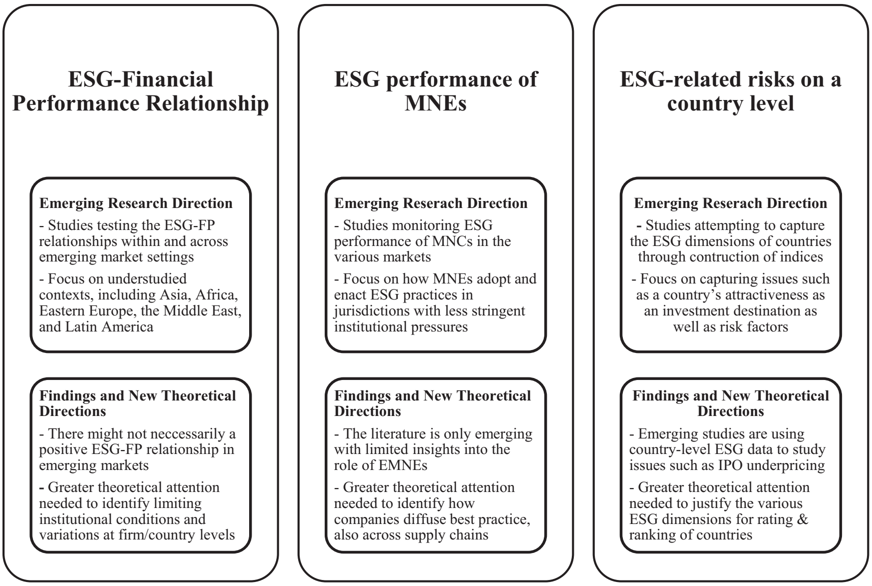

Figure 1. Emerging research on ESG in multinational business research

role of ESG and its contribution to value creation in Islamic finance (Paltrinieri *et al.*, 2020; Peng and Isa, 2020).

While this work has roots in confirming (and questioning) the validity of "Western" ESG-FP theory in emerging markets, it pays greater attention to limiting institutional conditions such as weaker governance, higher levels of political risk and/or heightened levels of corruption (Duque-Grisales and Aguilera-Caracuel, 2021). In addition, the literature also pays greater attention to variations within and across companies and countries by drawing on theories of national business systems, comparative capitalism and stakeholder engagement (Ortas *et al.*, 2019). Some studies replicate findings of generally positive associations between ESG and financial performance for developing country contexts (Bahadori *et al.*, 2021; Shakil *et al.*, 2019); However, several studies contradict this finding when focusing on emerging markets. For instance, Garcia *et al.* (2017) investigate the ESG-FP relationship for a sample of firms from BRICS countries. The authors analyze ESG ratings obtained from the Thomson Reuters Eikon database and report on a negative association of financial performance with environmental performance. A more recent study by Duque-Grisales and Aguilera-Caracuel (2021) focuses on the ESG-FP relationship of multinationals from Brazil, Chile, Colombia, Mexico, and Peru. The results point to a negative association between ESG ratings (also retrieved from Thomson Reuters) and multilatinas' financial performance. The authors conclude that this might result from the challenges and costs of implementing ESG initiatives in the setting studied, but also find a moderating effect of financial slack and geographic international diversification. These findings suggest that there is a much greater need to further study aspects such as agency problems and inefficient resource allocation in international settings.

Environmental, social and governance performance of multinational companies

A second, much smaller body of emerging work focuses on the ESG performance of multinational companies in the various markets in which these companies are operating (Park, 2018; Salsbery, 2021). This body of work examines how MNEs adopt and enact ESG practices across different markets and jurisdictions. The body of work has origins in theories on CSI and is based on concerns that ESG performance might be lower in jurisdictions with less stringent formal and social institutional pressures (Brammer *et al.*, 2021), thus leading to the assumption that emerging country contexts might place fewer demands on companies to adhere to superior ESG performance. However, prior research has primarily studied the companies headquartered in developed economies (particularly the USA) and the uptake of corporate sustainability practices (broadly defined) among international subsidiaries. The question of how the internationalization of emerging market multinationals (EMNEs) affects their ESG performance in other host countries has remained largely unexplored (Park, 2018), even though the internationalization of EMNEs has attracted attention in the literature (Gammeltoft *et al.*, 2012).

Recent work in this area (Salsbery, 2021) has further expanded on theory in the international business (IB) field by examining MNE's ESG behavior at home versus abroad, based on the location of its headquarters (in a developed versus developing economy). MNEs can choose to "export" the ESG norms and practices of the home market (the location of its headquarters) or can "adopt" norms and practices of the host market (location of foreign operations). Findings from the study by Salsbery (2021) show that MNEs headquartered in developed markets behave more irresponsibly in emerging markets than they do at home, while emerging market MNEs behave more responsibly when operating in developed markets. The study concludes that these results can be attributed primarily to governance (rather than social or environmental) factors. However, the main drivers behind MNE's and especially EMNE's engagement in ESG (as well as their ESG performance internationally and in the context of global supply chains) are still undertheorized. Factors such as organizational legitimacy to overcome the liability of foreignness have been explored for cross-listed companies and might play a role (Del Bosco and Misani, 2016), but further research is needed to understand their impact in the context of ESG. There is limited research that focuses on the diffusion of ESG practices within and across MNEs, and research has not yet documented if factors such as firm size, industry or home/host country factors accelerate or hinder the diffusion of ESG practices.

Frameworks for assessing environmental, social and governance-related risks on a country level

In addition to firm-level ESG ratings, studies also focus on analyzing the ESG dimensions of countries. Dyck *et al.* (2019), for example, construct a data set reflecting country-level ESG norms based on data from the Environmental Performance Index (measuring country-level data on health and ecosystem vitality) and the World Values Survey (assessing peoples' values and beliefs). Using the country-level data set as a proxy, Dyck *et al.* (2019) conclude that institutional investors from countries with strong norms have a positive impact on companies' ESG policies. Increasingly, ESG rating providers that have traditionally offered scores at the corporate level are now also focusing on providing country-level ESG data (e.g. MSCI's ESG Government Ratings which quantify a country's exposure to ESG risk-weighted against the management of the risk), primarily with the view to rate a country's attractiveness as an investment destination and to extend the insights offered by traditional analyses of sovereign debt and a country's creditworthiness (MSCI, 2020). In addition, data have also been made available by the World Bank in the form of an ESG Data Framework. The framework offers ESG data on country, regional and global levels for issues such as emissions and pollution, poverty and inequality or human rights, and is linked to the sustainable development goals (SDGs) [2].

Researchers have started to use these country-level ESG data sets in various contexts, for instance, to study IPO underpricing in countries with different ESG ratings (Baker *et al.*, 2021). Alternative metrics are provided by companies such as RepRisk - the RepRisk Country ESG Risk Index quantifies business conduct risk exposure related to country-level ESG issues – it is therefore technically not a country-level ESG rating but a business risk assessment. However, analyses of country-level ESG scores have raised some concerns that they might lead to potentially biased insights. For instance, a report by the World Bank Group (Gratcheva *et al.*, 2020) found strong correlations between national income and the ESG pillars, which the report refers to as "ingrained income bias" (p. 31). Consequently, country-level ESG scores might be biased toward "richer" countries with higher prosperity, which could result in a misallocation of capital to wealthier countries. While scores can certainly be adjusted to account for this bias, the report voiced concern that the measurement of country-level ESG risk might therefore not fully reflect sustainable investment opportunities and calls for greater methodological transparency around these issues.

Discussion and future research

While the emerging body of work adds an important dimension to the identification and awareness of ESG issues globally, numerous unresolved issues become evident (Figure 2). First, the increasing popularity of ESG ratings has primarily originated in developed countries, meaning that ESG frameworks have been built to assess corporate sustainability

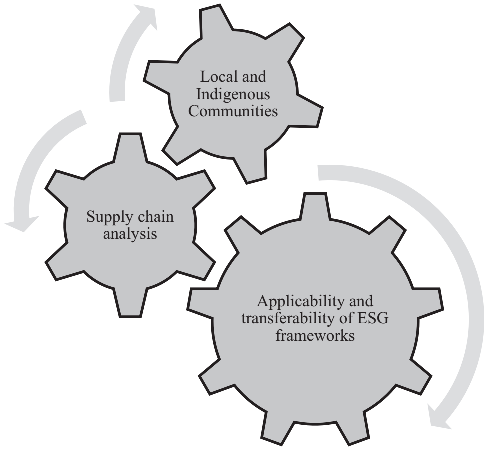

Figure 2.
Areas for future research

as it relates to firms in their "home" countries. Due to their origins, ESG scores have been primarily developed for companies listed on US or European/UK stock exchanges, meaning that ESG frameworks have been tied to a company's listing in these markets. This has important implications, for instance, regarding the applicability and transferability of these frameworks to study ESG in emerging markets. While ESG ratings are now being developed for a larger number of markets, research has shown that ESG scores for firms in emerging markets are subject to bias and are not weighted by materiality, which can be misleading for using the data in research but also in portfolio construction and performance (European Centre for Corporate Engagement, 2016; Mobius and Ali, 2021). Similar issues also apply to country-level ESG scores, as discussed above. Second, while ESG scores (depending on the data provider) do factor in international firm activities (e.g. Human Rights and Child Labour Policies) these are often not captured in detail and not mapped across the corporate supply chain where ESG issues are prone to happen. Third, ESG scores do not integrate views and voices from various local stakeholders that are impacted by firm activities, especially Indigenous communities (Pelosi and Adamson, 2016). These issues are further discussed in the following sections.

While there are certainly calls to consolidate and standardize ESG information to address the above-mentioned discrepancies, Eccles and Stroehle (2018) raised the valid point that full convergence on ESG issues and measurements is unlikely given the development of proprietary rating systems by individual data vendors. This raises the perhaps broader question of to what extent information captured through private market-based approaches can reflect ESG in emerging markets. Ho and Park (2019) seek to answer this question by comprehensively reviewing issues associated with private market-based approaches to ESG disclosure across South Africa, Brazil, the USA, the EU, the UK, Hong Kong and mainland China. The authors detail the complex nature of ESG disclosure requirements (including each jurisdiction's legal and institutional framework and interactions of public regulation with private ESG disclosure frameworks) suggesting that a public–private hybrid approach to ESG disclosure might ultimately be inevitable if more consistent and comprehensive disclosures are meant to be achieved. However, for purposes of advancing research (and industry practice) in this area, it is perhaps of more immediate importance to identify possible issues and shortcomings associated with using ESG ratings in cross-country studies and for assessing the performance of multinational enterprises (MNE) and emerging market multinationals (EMNEs). This will allow research and practice to move forward with more nuanced inquiries and with frameworks that are not solely based on Western norms.

Applicability and transferability of environmental, social and governance frameworks

As detailed in the introduction, the rapidly increasing area of SRI has sparked a substantial scholarly debate regarding whether higher ESG-related performance is helping to generate value for both shareholders and stakeholders impacted by firms' ESG practices. As this article has shown, this question is now increasingly being investigated in emerging markets, but findings have remained inconclusive. Prior research has already pointed to several empirical challenges associated with studying the ESG–FP relationship: Studies have used different ESG definitions and metrics which had created difficulties in arriving at definite conclusions (Eccles and Stroehle, 2018; Whelan *et al.*, 2020). The inclusion of other variables such as different moderating and control variables (or lack thereof) can further obscure the "true" relationship between ESG-related performance and financial performance (Carroll and Shabana, 2010; Margolis *et al.*, 2007). As identified above, there is a likely need to further study aspects such as agency problems and inefficient resource allocation as they relate to the uptake of ESG initiatives in emerging markets. In addition, prior research has used different samples (e.g. in terms of industry focus, timeframes and so on), and has also used different financial performance measures (ranging from various "rate of return" measures to the use of market returns, Beck *et al.*, 2018; Orlitzky *et al.*, 2003), thus making comparisons of findings across sectors and countries difficult. These issues will require consideration in research in emerging market contexts, especially for studies seeking to compare companies' ESG performance across different contexts.

Studying the ESG–FP relationship in emerging markets faces additional challenges due to less stringent disclosure environments and lower levels of transparency (Bahadori *et al.*, 2021; Hoang, 2018). Mobius and Ali (2021) offer a discussion of difficulties associated with assessing ESG-related performance at the firm level in emerging markets and describe different cases in which ESG ratings failed to accurately identify a firm's ESG performance. The main point that Mobius and Ali (2021) raise concerns *disclosure practices*: The authors identify a company that received a mediocre ESG rating by a well-known ESG rating provider, mainly because it was ranked as an ESG laggard for its sourcing practices. However, further analysis suggested that the company received a low score as it was not disclosing its policies and statements – which might not have been an accurate reflection of the company's actual ESG performance and actions. In this instance, the ESG scores may have rather ranked the existence of ESG-related disclosures. A fundamental problem is not just related to data availability and reliability but also to the ability to "export" ESG frameworks to assess ESG in different contexts that are characterized by vastly different cultural and contextual factors (Elg *et al.*, 2017). At the aggregate level, ESG scores for firms in emerging markets were found to be impacted by size, sector and country (location) biases, meaning that ESG scores can vary substantially when considering these factors (European Centre for Corporate Engagement, 2016). Similar issues arise for country-level ESG scores, as discussed above.

Other issues relate to the ability of ESG ratings to *"detect" corporate governance failures* and to capture *issues of materiality* in emerging markets. Regarding the detection of governance failures, Mobius and Ali (2021) detail a case from India's banking sector where ESG ratings did not accurately flag concerns about poor corporate culture and lending practices. This issue does arguably not only apply to ESG ratings in developing markets. For instance, a study by Utz (2019) found that aggregated ESG scores cannot be used as reliable proxies for forecasting the likelihood of corporate scandals, which is primarily due to the retrospective analysis of companies' ESG practices. Future research will be required to answer questions such as to what ESG scores can be used for assessing credit scores or risk governance in emerging markets, and how they can be weighted to account for the individual circumstances of a firm. Regarding the ability to capture issues of *materiality in emerging markets*, the question arises if all issues that are captured by ESG frameworks are indeed driving the ESG performance of companies in emerging markets. The issue of materiality is a key concept in the accounting discipline and refers to the significance that is ascribed to data and information (and the omission thereof) in the decision-making process. An example might illustrate this point – reductions in a firm's carbon emission levels are likely to have a significant impact on risk-adjusted return for firms in material-intensive industries, but not in other industries (e.g. professional services) (LaBella *et al.*, 2019). Similarly, for companies in emerging markets, some of the E, S and G dimensions are likely to face key sustainability issues that present risks and drive performance, for instance in areas such as supply chain risks (Odell and Ali, 2016, see also discussion below). Further research can assess how materiality can be determined and factored into the ESG assessment process.

Supply chain analysis

A second underexplored area concerning the use of ESG ratings in multinational business research is the mapping of ESG activities across home and host country activities, and especially across corporate supply chains. For large global companies, the distinction between being headquartered in a developed versus developing country might increasingly be less relevant given the global extent of many companies and their operations. However, a key challenge for these companies is to comprehensively track their supplier networks and to be able to map out and understand the ESG performance of not only the suppliers but also the suppliers of suppliers, and so on (i.e. examining multiple tiers). Often, significant ESG risks are lower down in supply chains, for example, a factory associated with forced labor might be involved at some stage in the fashion supply chain, but unless the poor practices within the factory are uncovered and the involvement of the factory within the supply chain is made visible, it would largely go undetected. This leads to an increasing interest to incorporate a wider ESG lens into procurement decisions. Various IB scholars have already proposed that research needs to pay greater attention to MNEs' governing role within and beyond global supply chains to lessen governance inadequacies – for instance, concerning modern slavery, human rights and working conditions (Caruana *et al.*, 2021; Burmester *et al.*, 2019; Stringer and Michailova, 2018), but also issues such as corruption (Stevens and Newenham-Kahindi, 2021). This will have a direct impact on the availability of data and frameworks for the ESG context as well.

Some prior research has offered some theoretical observations regarding the challenges of managing and monitoring corporate activities across supply chains. For instance, a study by Kim and Davis (2016) tracking supply chain sustainability finds that firms with a greater level of diversification as well as larger and more dispersed supply chains found it more difficult to track the provenance of their products (in this case, conflict minerals). Further theory development is required to adequately conceptualize ESG issues in supply chains, also considering the commonalities and distinctiveness of various issues (Caruana *et al.*, 2021). Underlying issues related to gathering and analyzing data are not easy to address and will require novel approaches to track ESG especially also among small and medium-sized firms that might be operating internationally or might be embedded in international supply chains, but are not producing any ESG disclosures. Some ESG ratings providers are now offering customized solutions to track ESG issues among corporate supply chains, which is often based on manual data searches. Research has recently also expanded to examine how novel technological solutions including blockchain applications can be implemented across supply chain systems to help trace the provenance of goods and thus enforce integrity (Berdik *et al.*, 2021). However, this work is still at an early stage and will require further development before reliable ESG data can be derived.

Local and indigenous communities

A third underexplored area concerning the use of ESG ratings in multinational business research is the treatment of issues of importance to local and indigenous communities within ESG ratings. While some companies selling to governments (e.g. infrastructure projects) have faced contractual requirements to engage local communities and supplies and needed to report on the scope of the engagement, there is now increasing awareness amongst policy-makers, investors, and corporate decision-makers that many companies face significant ESG impacts from local community engagement. A study by Newenham-Kahindi (2015) on the implementation of sustainable development programs by MNEs across rural communities in Tanzania documents the challenges of implementing locally oriented strategies that incorporate meaningful employee and community engagement, which also means that MNEs need to overcome their liability of foreignness (Newenham-Kahindi and Stevens, 2018). Pelosi and Adamson (2016) draw further attention to the challenges faced by Indigenous communities and argue that there is a need to better manage the "S" in ESG. The authors discuss findings from an Indigenous Rights Risk Report in 2014, which assessed the security filings of 52 publicly listed US oil, gas, and mining companies to identify potential violations of indigenous peoples' rights. The report examined 330 international projects operated by these companies on or near indigenous land, finding that 35% (115) of projects had a high risk of Indigenous community opposition or violations of indigenous peoples' rights, 54% (177) had medium risk exposure, and only 11% (38) had low-risk exposure. The main issues identified were inadequate governance and oversight by corporate boards, but also the lack of data and insights for appropriate engagement.

Some ESG rating providers assess a firm's policy on Indigenous people, usually involving land rights. For instance, ESG rating provider Sustainalytics includes society and community-related controversies or incidents in its ESG ratings and evaluates if a company has a "Policy on Indigenous people and land rights". Indictors by ESG rating provider MSCI KLD assess concerns and strengths regarding a firm's approach to "Indigenous Peoples' Relations", examining if a company has established relations with indigenous people in areas where proposed or current operations take place. Other ESG rating providers, such as Refinitiv and Bloomberg, have no specific indicators for indigenous issues. Instead, Refinitiv assesses if a company is involved in ethical issues controversies, while Bloomberg assesses the amount of community spending such as donations to the local community.

Further research can strengthen current ESG approaches by examining ESG issues of importance to the various indigenous communities within and across countries. For instance, current ESG ratings are not considering how firms treat cultural artefacts of importance to local communities. The controversy surrounding mining giant Rio Tinto illustrates this point – the company was responsible for the destruction of the Juukan Gorge caves, a 46,000-year-old sacred Aboriginal site in Australia's Pilbara region, in 2020. While the destruction was technically legal and the company received permission for the demolition under (outdated) laws, it refused to update its plan when the archaeological importance of the site became clear. The incident also revealed a substantial disconnect between Rio Tinto's public commitments to responsible mining, and Aboriginal land rights, and its actions. The destruction was deeply traumatic for the Aboriginal population who lost an important cultural site. As evident from this example, there is scope for multinational business research to move beyond home and host country advantages to further examine how companies relate to indigenous country and indigenous people.

Conclusion

The paper identifies emerging literature that has started to focus on tracking the development and uptake of ESG ratings in the international context. It discusses three emerging research streams: Research examining the ESG-FP relationship in emerging markets, research tracking the ESG performance of MNEs and EMNEs in the various countries and regions they are operating, and frameworks for assessing ESG-related risks on a country level. While the emerging body of work adds an important dimension to the identification and awareness of ESG issues globally, numerous unresolved issues become evident. ESG frameworks have been built to assess corporate sustainability as it relates to firms in their "home" countries (typically with a focus on developed countries), with limited applicability and transferability to emerging markets. International firm activities are often not captured in detail and not comprehensively mapped across firm subsidiaries and a firm's corporate supply chain (where ESG issues are prone to happen), and ESG scores do not comprehensively integrate views and voices from various local stakeholders that are impacted by firm activities, including indigenous communities.

Notes

1. Ratings providers do typically provide some adjustments for companies operating in different geographical and cultural contexts, and provide adjustments (e.g. relative to industry peers). However, ESG frameworks and rating schemes have largely been created based on Western standards. Eccles and Stroehle (2018) provide a more in-depth discussion of how the background and origins of ESG ratings providers have likely shaped their priorities in measuring ESG.
2. See https://datatopics.worldbank.org/esg/ for a full description of the ESG indicators and data sets.

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