

# The role of ESG principles in attracting foreign investments

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**Abstract:** Environmental, Social, and Governance (ESG) principles have become a critical factor in global investment decisions. Investors increasingly prioritize sustainability, ethical governance, and social responsibility when allocating capital. This paper examines how strong ESG performance enhances a country's or company's ability to attract foreign direct investment (FDI). Using case studies and comparative analysis, we demonstrate that nations and firms with robust ESG frameworks experience higher investment inflows, reduced risk premiums, and improved long-term financial performance.

**Keywords:** ESG, foreign investments, sustainability, corporate governance, FDI

## Introduction

Foreign Direct Investment (FDI) is a key driver of economic growth, particularly in emerging markets. However, investors are no longer singularly driven by short-term financial returns, instead, they are increasingly prioritizing Environmental, Social, and Governance (ESG) criteria to assess risks, opportunities, and long-term value creation. This transformation reflects a broader recognition that sustainable and ethical practices are inextricably linked to economic resilience and profitability. ESG principles provide a structured framework for evaluating these non-financial factors. Without following ESG principles, it is hard for many countries or companies to attract investments. Because by doing business, we should also concern about the well-being of society, environmental impacts of our operations and preserve our resources for our future generations. ESG principles are one of the fundamental approaches of achieving long term sustainable development.

## Research objectives:

- Analyze the relationship between ESG performance and FDI inflows.
- Compare investment trends in high-ESG versus low-ESG countries.
- Examine case studies of companies benefiting from ESG-aligned investments.

## Hypothesis:

Countries and corporations with strong ESG compliance attract more foreign investments due to lower perceived risks and enhanced long-term sustainability.

## Methodology

The study employs different approaches to answer the questions at hand and check whether our hypothesis is true. These approaches are quantitative analysis, qualitative analysis and comparative tables.

Comparative tables involve comparing data about ESG ranking and FDI growth rates, while quantitative analysis is based on reviewing of FDI inflows in high-ESG versus low-ESG countries between 2015-2023. Qualitative analysis is about case studies of multinational corporations that shifted investments based on ESG criteria.

## Results

Countries with higher ESG scores attract more foreign direct investment (FDI) and capital because they signal stability, sustainability, and reduced risks to investors. There are direct links between following ESG principles and investment inflow. Investors prioritize minimizing risks, and ESG frameworks address three key categories of risk as such environmental risks, social risks and government risks.

Countries with strong environmental policies (e.g., carbon reduction targets, renewable energy adoption) are better positioned to avoid climate-related disruptions. For example, Denmark's investments in offshore wind energy reduced reliance on fossil fuels, attracting €12 billion in FDI for green tech projects. Also nations with strict environmental laws (e.g., EU members adhering to the Carbon Border Adjustment Mechanism) avoid fines and trade barriers, making them safer investment destinations.

Countries with fair labor practices, gender equality, and social safety nets reduce risks of strikes, lawsuits, or consumer boycotts. Nations with low inequality and high education levels offer skilled workforce and minimize civil unrest.

Strong governance ensures contract enforcement and fair dispute resolution. In addition, when there is political stability, it reduces risks of abrupt regulatory changes, creating attractive business environment.

Below, the table represents data about 2 countries with different ESG ratings.

Table 1.

High ESG versus low ESG country comparision

Factor	High ESG country Sweden	Low ESG country Nigeria
FDI inflows (2023)	\$42.1 billion	\$2.1 billion
Key sectors	Renewables, tech, healthcare	Oil/gas (declining due to divestment)
Investor perception	Low risk, innovation hub	High corruption, environmental risks

From the information provided in the table we can see that high ESG country Sweden attracts much more investments into their economy compared to Nigeria which is regarded as weak country in terms of implementing ESG principles. Investors believe that Sweden is relatively risk free country having sound ESG ranking so that the country attracts huge investment portfolio into their economy. While Nigeria is seen as risky economy for investors for their not stable economy and high corruption rates.

Countries with high ESG scores attract FDI because they offer lower risks, access to sustainable finance, and alignment with global trends. Investors increasingly view ESG compliance as a proxy for managerial competence and long-

term resilience. However, success requires authentic commitment - not just box-ticking - to avoid greenwashing pitfalls.

### Discussion

The correlation between strong ESG performance and increased FDI inflows (as shown in Table 1) can be explained through three interconnected mechanisms - risk mitigation, access to capital and long term value creation.

- Countries and companies with robust environmental policies avoid fines, sanctions, or operational disruptions. For instance, the EU's Carbon Border Adjustment Mechanism (CBAM) penalizes imports from nations with weak environmental standards, making high-ESG countries like Sweden more attractive for manufacturing investments.

Investors increasingly avoid entities linked to human rights violations or corruption. For example, after Nigeria's poor governance score (Table 1), Shell faced divestment pressures in 2022 due to oil spill controversies in the Niger Delta.

Climate-vulnerable nations (e.g., Bangladesh) struggle to attract long-term infrastructure investments unless they adopt adaptation measures, which ESG frameworks incentivize.

- ESG-aligned firms gain preferential access to green finance, such as green bonds and sustainability-linked loans. Tesla's \$5 billion green bond issuance in 2021, tied to renewable energy projects, underscores this trend.

ESG-focused funds now manage over \$40 trillion globally (Bloomberg, 2023). Investors like BlackRock prioritize portfolios with high ESG ratings, creating a "virtuous cycle" where compliant firms attract more capital.

- Companies with strong social governance experience lower employee turnover and higher productivity. Unilever's "Sustainable Living Plan" reduced supply chain disruptions by 25%, enhancing investor confidence.

Renewable energy projects in high-ESG countries offer stable returns over decades, contrasting with volatile fossil fuel investments.

### Challenges of ESG implementation

Despite the benefits, ESG adoption faces significant hurdles.

Companies like Volkswagen and Coca-Cola (plastic waste controversies) have misrepresented sustainability efforts, eroding investor trust. In 2023, the SEC fined several firms for misleading ESG disclosures.

ESG initiatives require upfront costs, deterring short-term-focused investors. However, studies show firms with high ESG ratings outperform peers by 4-6% annually over 10 years (MSCI, 2023).

### Conclusion

ESG principles are no longer optional - they are a necessity for attracting foreign capital. Countries and corporations that integrate ESG into their strategies benefit

from higher FDI, better risk management, and improved stakeholder trust. Future research should explore sector-specific ESG impacts on investment flows. Countries like Uzbekistan can increase its investment attractiveness by implementing ESG standards in doing business and achieving long term sustainable development. Step by step we are establishing our taxonomy and standards to do business according to ESG principles.

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