

Localizing ESG Theory in China: Policy Evolution and a Four-Tier Theoretical Framework

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Abstract

As the world's second-largest economy with strong state leadership, China plays a pivotal role in global sustainability. Yet, ESG development remains constrained by a lack of theory-driven research suited to its institutional context. This study proposes a localized, policy-oriented ESG framework. Based on a Systematic Literature Review (SLR) and Latent Dirichlet Allocation (LDA) topic modeling of ESG policy documents (2014-2024), we identify key theories and map them onto China's three-stage ESG policy evolution. The resulting framework offers theoretical and methodological guidance for China and provides insights for ESG localization in other emerging markets, highlighting China's potential in ESG innovation and global governance.

Keywords: ESG, China, Policy-oriented Framework, Emerging Markets, ESG Localization

Introduction

Since its introduction by the UN in 2005, ESG has become a prominent research domain. In China, despite increasing policy support (Tang & Jin, 2023), ESG implementation faces persistent challenges, including low disclosure quality, limited corporate awareness, and greenwashing (He, 2023; Zeng et al., 2024). These issues hinder progress toward the Dual-Carbon Strategy and weaken sustainable financial development. A key reason lies in the mismatch between imported ESG frameworks and China's institutional context. Although concepts like "Common Prosperity" and "Green Development" echo ESG principles, their integration remains complex and fragmented. While Chinese scholarship has examined ESG drivers, ratings, and outcomes, its theoretical underpinnings remain weak. ESG research lacking robust theory risks limited credibility and impact (Huang, 2021). Predominantly Western ESG theories - shaped by developed markets - struggle to align with China's policy-led environment and unique governance structures. This divergence underscores the need for a localized ESG framework that reflects domestic realities while supporting global sustainability goals.

This study attempts to bridge this gap by developing a four-tier ESG theoretical framework tailored to China's capital markets. Drawing on a Systematic Literature Review (SLR) and Latent Dirichlet Allocation (LDA) modeling, it integrates theoretical and policy insights. The SLR (CNKI, Web of Science, Scopus) traces ESG theory development in Chinese scholarship. Based on three policy stages - Nascent, Exploration and Development, and Deepening and Optimization - LDA is applied to analyze policy discourse. The resulting framework reflects China's institutional context, governance priorities, and regulatory evolution. The study explores three questions: (1) What theories underpin ESG research in China? (2) How has the ESG policy ecosystem evolved? (3) How can a policy-driven ESG framework be developed for China?

This study offers three key contributions. First, it conducts a systematic literature review to consolidate 14 ESG-related theories in Chinese scholarship, addressing the absence of localized theoretical foundations. Second, it applies LDA topic modeling to trace the evolution of China's ESG policy discourse, providing a replicable method for linking policy and theory in emerging markets. Third, it proposes the Core-Global-Market-Social (CGMS) framework, which restructures mainstream ESG theories by integrating state capacity and socialist governance - dimensions often overlooked in Western models - thus aligning global ESG concepts with China's institutional context.

Systematic Literature Review

The SLR approach distinguishes itself from traditional literature reviews through its rigorous multi-stage protocol, which encompasses systematic retrieval, standardized screening, and critical appraisal of studies. This structured approach minimizes selection bias while synthesizing robust evidence to address specific research questions (Hammersley, 2002).

Literature Search and Selection

To ensure methodological rigor, this study followed a four-stage SLR process (Figure 1). First, the research scope was defined and screening criteria established (Table 1), limiting inclusion to peer-reviewed journal articles in English and Chinese from 2014-2024. Second, a systematic search was conducted across Web of Science (SSCI), Scopus, and CNKI using bilingual ESG-related keywords, yielding 93 articles after removing duplicates and irrelevant records. Third, 70 articles were selected after full-text screening for theoretical relevance. Finally, these were synthesized to extract key insights and construct the theoretical framework.

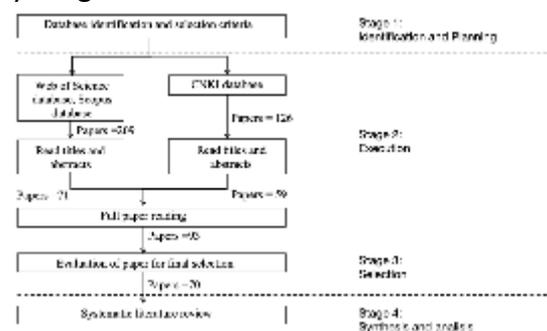


Figure 1. Systematic Literature Review Research Protocol

Table 1

Articles inclusion and exclusion criteria

Criterion	Decision
Duplicates within the searched documents	Excluded
Full text available in a digital database	Included
Type of articles: research articles	Included
Published in a scientific, peer-reviewed journal	Included
Type of articles: conference proceedings, review articles, book reviews, books, book chapters, and others	Excluded
Predefined keywords exist as a whole or at least as part of the title, keywords, or abstract section of the paper	Included

Key Findings and ESG Theory

From 2022 to 2024, theoretical ESG research in China grew rapidly, accounting for more than half of all reviewed studies. In contrast, publications from 2014 to 2021 showed limited theoretical engagement. Compared with international scholarship, Chinese studies place greater emphasis on ESG theory - likely influenced by national policy shifts, particularly the launch of the Dual Carbon Goals in 2020, which intensified focus on ESG frameworks.

Across all reviewed studies, ten key theoretical frameworks emerged, with Stakeholder Theory cited most frequently, followed by Signaling Theory and Sustainable Development Theory (Table 2).

Table 2

Top 10 Theories with the Highest Citation Frequency

Theory	Number of Citations
Stakeholder Theory	32
Signaling Theory	14
Sustainable Development Theory	12
Institutional Theory	11
Information Asymmetry Theory	9
Agency Theory	8
Social Responsibility Theory	7
Resource-Based Theory	6
Reputation Theory	5
Resource Dependence Theory & Economic Externality Theory	4

Comparison of the top ten ESG-related theories in international and Chinese articles shows Stakeholder Theory as the most frequently cited in both groups (Table 3). This indicates that, across contexts, ESG development fundamentally centers on corporate–stakeholder relationships, highlighting the role of firms in addressing the expectations of shareholders, employees, customers, governments, and others.

Table 3

Comparison of Top 10 Theories in International and Chinese ESG Research

International	Chinese
Stakeholder Theory	Stakeholder Theory
Institutional Theory	Signaling Theory
Agency Theory	Information Asymmetry Theory
Resource-Based Theory	Sustainable Development Theory
Sustainable Development Theory	Social Responsibility Theory
Signaling Theory	Economic Externality Theory
Legitimacy Theory	Responsible Investment Theory
Sustainable Finance Theory	Modern Corporate Governance Theory
Reputation Theory	Resource Dependence Theory
Social Learning Theory & Organizational Learning Theory & Dynamic Competition Theory	Reputation Theory & Green Investment Theory

To build a coherent ESG theoretical framework, this study first identified the ten most cited theories in Chinese literature and incorporated Institutional Theory, Agency Theory, and Resource-Based Theory from international research to enhance contextual relevance. As current studies often rely on fragmented, discipline-specific theories, this study integrates them into four conceptual layers - Core, Market, Social, and Global (Figure 2) - based on their primary focus. This layered structure addresses theoretical fragmentation and aligns ESG research with China’s policy-driven institutional landscape.

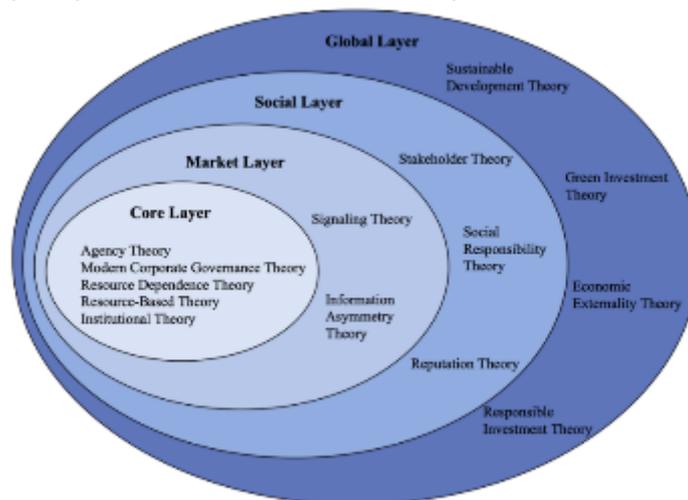


Figure 2. Theoretical Framework of ESG

The Core Layer underpins ESG by drawing on Agency, Corporate Governance, Resource Dependence, Resource-Based, and Institutional theories. These emphasize internal governance and strategic alignment with institutional pressures. Ownership-control separation creates agency risks, requiring self-regulation to protect shareholder interests (Ahmed et al., 2024; Ni et al., 2024). Governance also involves stakeholder engagement and value co-creation (Hu et al., 2023). Embedding ESG metrics into strategy strengthens competitiveness and long-term resilience (Moussa et al., 2024).

The Market Layer bridges corporate governance and market dynamics, drawing on Signaling and Information Asymmetry theories. ESG disclosures communicate sustainability

strategies to stakeholders lacking internal access - investors, consumers, and regulators - thus reducing information gaps and improving transparency (Chen et al., 2023; Wang & Xie, 2022). Stakeholder responses - via investment, consumption, or regulation - form a feedback loop that shapes firms' ESG strategies. This bidirectional signaling refines corporate sustainability efforts and enhances market reputation.

The Social Layer reflects the societal dimension of ESG, highlighting firms' responsibilities beyond profit. Informed by Stakeholder, Social Responsibility, and Reputation theories, it emphasizes ESG's role in shaping CSR and corporate reputation. As SDGs gain traction, stakeholders expect firms to deliver both economic and social value (Son & Suh, 2024). To align with these expectations, companies adopt proactive CSR strategies - such as responsible supply chains and green innovation - to build trust, enhance competitiveness, and reinforce social legitimacy (Zhang et al., 2024).

The Global Layer reflects the macro dimension of ESG, highlighting its transnational and systemic relevance. Informed by Sustainable Development, Green Investment, Externality, and Responsible Investment theories, it emphasizes how firms internalize environmental costs and support global sustainability efforts. As green growth becomes integral to development, stakeholders increasingly promote eco-friendly investment, production, and consumption. ESG thus aligns environmental responsibility with economic goals, advancing both profitability and sustainability (Xing, 2017), and reinforcing its role in inclusive, long-term stewardship.

ESG Policy Evolution in China

China's ESG policies encompass diverse themes. To analyze them, this study employs LDA topic modeling, a machine learning method that uncovers latent patterns in policy texts by assigning topic probabilities (Blei & Jordan, 2003). This enables systematic identification of discourse trends and shifts in regulatory priorities.

Determining the Optimal Number of Topics

China's ESG policy evolution comprises three stages: Nascent (2002–July 2016), Exploration and Development (Aug. 2016–Sept. 2020), and Deepening and Optimization (Oct. 2020–2024) (Dong et al., 2024). Based on this, 56 screened policy documents were collected via Baidu. Using Python, preprocessing included stop-word removal (snowball method), Jieba segmentation, and LDA modeling via Gensim. Optimal topic numbers were selected by balancing perplexity and coherence score: six, five, and seven topics were set for the three stages respectively.

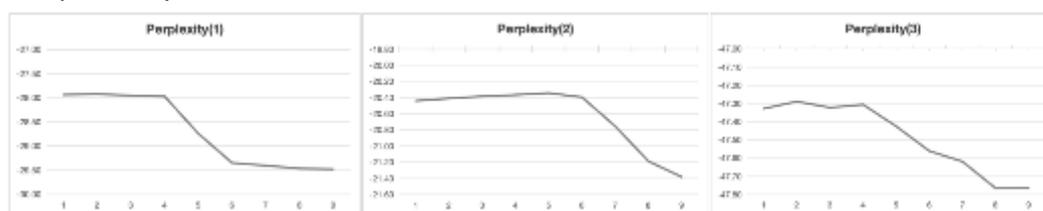


Figure 3. Line Chart of Topics vs. Perplexity

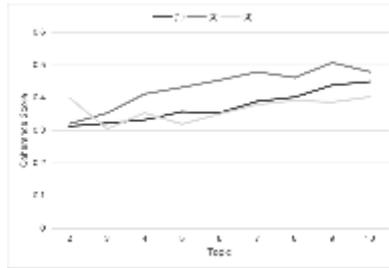


Figure 4. Line Chart of Topics vs. Coherence Score

Analysis of Theme Intensity and Evolution

By focusing on probabilistic word distributions and intensity values, the analysis reveals shifts in policy attention.

Table 4

Nascent Stage

Number	Intensity	High-Probability Keywords
Topic1	0.1685	Shareholder, Commitment, Actual, Director, Variety
Topic2	0.1672	Environmental Protection, Related, Management, Report, State
Topic3	0.1666	Implementation, Including, Audit, Report, Transaction
Topic4	0.1662	Environment, Environmental Protection, Internal, Unit, Disclosure
Topic5	0.1659	Raising Funds, Investment, Verification, Pollutant, Issuance
Topic6	0.1657	Director, Supervisor, Managerial Staff, Society, Procedure

The coherence score of 0.3279 indicates moderate semantic consistency, aligning with the exploratory nature of China’s early ESG policies. During this nascent stage, policies were top-down and compliance-oriented. LDA results highlight themes like shareholder duties, board governance, and environmental protection. Keywords such as “audit,” “report,” and “disclosure” suggest early efforts focused on institutional awareness and basic reporting, with ESG not yet integrated into core strategy. Balanced topic intensities reflect a fragmented but emerging policy landscape.

Table 5

Exploration and Development Stage

Number	Intensity	High-Probability Keywords
Topic1	0.2001	shareholder, guarantee, director, strengthening, operation
Topic2	0.2000	fund, shareholder, reason, work, development
Topic3	0.2000	market, investment, responsibility, management, service
Topic4	0.1999	investment, environment, development, promotion, China
Topic5	0.2000	shareholder, controlling stake, director, semi-annual, investor

In this stage, China’s ESG policy became more institutionalized, reflected in a higher coherence score (0.4780) and clearer thematic focus. Keywords like “investment,” “responsibility,” “environment,” and “director” point to growing attention to sustainability and accountability. Yet, engagement remained symbolic, with terms like “shareholder,” “guarantee,” and “controlling stake” emphasizing formal governance over substance. The absence of terms such as “transparency” or “standardization,” along with even topic intensities, suggests ESG disclosure was still compliance-oriented, not strategically embedded.

Table 6

Deepening and Optimization Stage

Number	Intensity	High-Probability Keywords
Topic1	0.1352	Evaluation, Goal, Energy, Implementation, Model
Topic2	0.1027	Entity, According to Law, Market, Process, Quality
Topic3	0.1288	Product, Asset, Limited To, Existence, Project
Topic4	0.1763	Development, Sustainability, Management, Finance, Importance
Topic5	0.1616	Emission, Greenhouse, Gas, Governance, Institution
Topic6	0.1297	Business, Operation, Industry, Main, Measure
Topic7	0.1657	Risk, Climate, Environment, Opportunity, Significant

The coherence score for this stage is 0.3537, reflecting a moderate level of semantic consistency that corresponds to the more structured yet still evolving nature of ESG policy at this point. In the Deepening and Optimization Stage, China's ESG agenda aligned more closely with national goals like the Dual Carbon Strategy. Keywords such as "development," "sustainability," "evaluation," and "finance" signal strengthened institutional frameworks and emphasis on standardized disclosure. The rise of terms like "climate," "emission," and "risk" indicates increasing focus on environmental risk governance. However, the limited presence of "stakeholder" or "society" suggests social aspects remained marginalized. ESG practices, though more regulated, still prioritize compliance over proactive value creation.

China's ESG policy has progressed from early-stage regulatory guidance to more structured and strategic governance, driven largely by government initiatives. However, policies across the environmental, social, and governance pillars remain fragmented, with insufficient integration of social aspects. ESG practices are still compliance-oriented rather than value-driven.

Reconstructing ESG Theory in the Chinese Context

China's ESG system follows a government-led, policy-driven model (Zhang & Cai, 2023). While regulatory mechanisms for environmental governance, green finance, and corporate oversight are relatively mature, the social dimension lacks market-based incentives and systemic support. Due to strong state intervention and market asymmetries, Western ESG theories are not directly applicable. A localized ESG framework thus requires theoretical adaptation, coordinated policymaking, and mechanisms to balance social responsibility within China's distinct institutional context.

Four- Tier Theoretical Framework and ESG Policy Alignment

China's ESG policies are densely concentrated in the environmental (E) and governance (G) dimensions, while the social (S) dimension remains relatively weak. To systematically construct an ESG theoretical framework with Chinese characteristics, this study adopts the Core-Market-Social-Global framework to evaluate the alignment between theory and policy at each level (Table 7).

Table 7

Four-Layer Theory-Policy Mapping Table

Theoretical Layer	Dimension	Policy Intensity
Core Layer	G	High
Market Layer	E+G	Moderate
Social Layer	S	Low
Global Layer	E	High

Throughout the Nascent, Exploration and Development, and Deepening and Optimization stages, China's ESG policy has consistently prioritized the E and G dimensions, with the S dimension receiving comparatively less attention. The Core Layer emphasizes internal corporate governance, characterized by high policy intensity and a government-led approach. The Global Layer addresses global sustainable development issues critical to the Earth's ecosystem, such as climate change, carbon reduction, and biodiversity protection, aligning primarily with the E dimension. Since the introduction of China's Dual Carbon Goals, policy intensity in this area has significantly increased.

The Market Layer bridges China's capital market with the global financial system, covering both E and G dimensions. However, due to China's policy-driven ESG system and underdeveloped market mechanisms, policy intensity in this layer remains moderate. The Social Layer involves multiple stakeholders, including shareholders, regulators, employees, and the public. Despite the frequent mention of "shareholders" in policies, the focus is largely on enhancing corporate governance rather than addressing corporate responsibilities to broader societal stakeholders. Consequently, S-related policies remain underdeveloped, and a comprehensive social responsibility framework has yet to emerge.

Overall, China's ESG policy landscape is highly imbalanced, with significantly greater emphasis on G and E compared to S. Market mechanisms in both the G and E dimensions are still in the process of gradual improvement.

An ESG Theoretical Framework with Chinese Characteristics

This study establishes a Chinese-style ESG theoretical framework based on the Core-Global-Market-Social structure, reflecting the hierarchical strength of China's ESG policies and their interaction with ESG theory (Figure 5).



Figure 5. CGMS Theoretical Framework

China's ESG policies prioritize enterprises as core implementers, making corporate governance the foundation of the Core Layer. The Global Layer aligns domestic ESG efforts with international standards, guided by national strategies such as "a community with a shared future for mankind," enhancing global responsibility and international market integration. The Market Layer institutionalizes ESG within capital markets, combining investor demand with policy incentives. Beyond market mechanisms, under democratic centralism, ESG also serves national development and social well-being, embodied in the Social Layer. This CGMS framework reflects China's ESG progression - linking enterprise governance, global alignment, market regulation, and inclusive growth - offering a context-specific alternative to Western ESG models.

China's ESG development follows a "policy compliance-driven, market-adjusted" model, which represents the lowest-cost and most pragmatic approach at the current stage of ESG advancement. To address this, the Chinese ESG theoretical framework necessitates a fundamental revision of traditional ESG theories, incorporating compensatory mechanisms tailored to China's unique policy and market environment. Accordingly, this study reinterprets key ESG theories within four contextualized dimensions: *Core, Global, Market, and Social*.

Core Layer

Agency Theory: Reframed as a government–corporate dual agency model, where the government acts not only as a regulator but also as a key stakeholder in enterprises.

Modern Corporate Governance Theory: Replaced the traditional "shareholder primacy" logic with a tripartite structure involving political principals, market principals, and agents.

Institutional Theory: Emphasizes a unique institutional pressure, where enterprises must first achieve political compliance before engaging in market competition.

Resource Dependence Theory: Integrated into a policy-enabled resource allocation mechanism, including carbon trading markets and green credit systems.

Resource-Based Theory: Reinterpreted to position ESG capabilities as strategic assets, with green enterprises gaining preferential financing through policy support.

Global Layer

Sustainable Development Theory & Green Investment Theory: Merged into a policy–market hybrid model that supports sustainable growth through state-led green finance

instruments.

Economic Externality Theory & Responsible Investment Theory: Operationalized via mechanisms such as ecological compensation and pollution cost internalization, ensuring that negative externalities are addressed through regulatory and market responses.

Market Layer

Signaling Theory & Information Asymmetry Theory: Applied through a dual-track certification system that combines market-based ESG ratings with government-issued labels, creating two parallel but reinforcing channels of influence.

Social Layer

Stakeholder Theory, Social Responsibility Theory & Reputation Theory: Expanded into a dual response mechanism, where CSR activities such as rural revitalization and common prosperity are jointly promoted and rewarded by both the government and the market.

This Core-Global-Market-Social framework reconfigures the Western three-dimension model into one that reflects China's governance priorities, global alignment, market transition, and social development goals.

Case Study

Contemporary Amperex Technology Co., Limited (CATL), founded in 2011, is a global leader in power batteries and energy storage systems, and a core player in China's new energy strategy. Given its market influence and ESG policy sensitivity, CATL serves as a representative case. While it did not release CSR or ESG reports in its early years, it began CSR reporting in 2019 during China's ESG Exploration and Development Stage and transitioned to ESG reporting in 2021 as the country entered the Deepening and Optimization Stage-reflecting a delayed policy response. This study analyzes all available CSR and ESG reports from CATL using topic modeling, with model quality assessed via coherence score and perplexity. Ten optimal topics and their high-frequency keywords are presented in Table 8.

Table 8

Topic Modeling Results: Top Keywords and Topic Intensities

Number	Intensity	High-Probability Keywords
Topic1	0.1447	Supply Chain, ESG, Governance, Supplier, Performance
Topic2	0.1298	Safety, Governance, Society, Customer, Health
Topic3	0.1294	Activities, Society, Community, Training, Local
Topic4	0.1129	Emissions, Governance, Pollutants, Contaminants, Society
Topic5	0.0936	Safety, Risk, Training, Work, Internal
Topic6	0.0934	Base, Product, Battery, Governance, Factory
Topic7	0.0904	Battery, Integrity, Recycling, Training, License
Topic8	0.0734	Supplier, Supply Chain, Training, Audit, Requirements
Topic9	0.0685	Innovation, R&D, Battery, Product, System
Topic10	0.0639	Emissions, Gases, Governance, Greenhouse, Risk

Traditional ESG theories categorize issues into distinct Environmental, Social, and Governance domains, but corporate disclosures often blend these themes. For instance, Topic 2 includes governance, social, customer, and health terms, reflecting practical or compliance-driven reporting rather than strict theoretical boundaries. Topics 1 and 3 further suggest firms focus on operational themes like supply chains and community engagement. Unlike abstract,

value-based categories in Western theory, Chinese firms disclose ESG content based on business logic. CATL's delayed ESG reporting - beginning only in 2021 - also illustrates China's policy-driven ESG trajectory: policy guidance precedes market pressure and corporate compliance. This underscores the need for a localized ESG framework suited to China's institutional context.

At the Core level, keywords like "governance," "safety," and "integrity" reflect CATL's emphasis on internal control and compliance, aligning with China's dual-agent model where firms answer to both shareholders and the state. Institutional and governance theories thus require adaptation to this political-market context. At the Global level, terms such as "ESG" and "performance" indicate efforts to align with international norms via policy-market tools like green credit and carbon markets. At the Market level, supply chain terms (e.g., "supplier," "audit," "quality") show ESG disclosures framed around supplier management, producing a dual signaling effect - addressing both market and government expectations.

However, at the Social layer, the S dimension appears relatively weak. Although Topic 1 includes social responsibility keywords such as "community", "local", "activities" and "training", the intensity of this topic is relatively low. This suggests that the company treats social responsibility more as a supplementary action than as a core strategy. The limited strength of this dimension indicates that, in the absence of mandatory institutional enforcement, traditional theories such as stakeholder theory and reputation theory may lack sufficient influence. Strengthening social responsibility still requires a collaborative governance mechanism among the government, enterprises, and society.

In summary, CATL's ESG practices support the practical relevance of the CGMS framework. The company's disclosure behavior follows a logic of "political compliance first, alignment with global standards, response to market rules, and supplementary social responsibility".

Conclusion and Future Research Direction

Existing ESG research primarily focuses on empirical analysis, such as the relationship between ESG performance and firm value (Kumar & Firoz, 2022), the influence of ESG disclosure on investor decision-making (He et al., 2024; Li et al., 2024), and ESG rating methodologies (Liu, 2022). These studies draw heavily on classical theories in management and economics. However, limited attention has been paid to theoretical foundations, particularly localized ESG frameworks suited to specific national contexts. This gap weakens the explanatory power of empirical findings and limits the adaptability of mainstream ESG theories to emerging markets (Tuck & McKenzie, 2014).

Unlike prior studies that treat ESG as a static, universal construct and focus primarily on empirical validation, this study emphasizes theoretical reconstruction grounded in national institutional contexts. Using SLR and LDA modeling on 70 articles from WOS, Scopus, and CNKI, it identifies 14 influential ESG theories and develops a localized, four-dimensional CGMS framework (Core, Global, Market, Social). This framework reflects China's policy-market-enterprise interplay, where ESG disclosures are shaped more by external mandates and adaptive responses than intrinsic value alignment. LDA analysis of policy texts reveals a regulatory emphasis on Governance and Environmental dimensions, with Social factors

consistently marginalized - underscoring a state-led, compliance-driven ESG logic. The CATL case further substantiates the CGMS model by mapping corporate disclosures to its four dimensions across policy phases. This study reframes ESG theory through a mechanism-oriented, context-sensitive lens, contributing a conceptual foundation that captures the dynamics of ESG institutionalization in China and offers a transferable framework for other emerging economies navigating similar structural asymmetries.

Future research should empirically test the CGMS framework using firm-level ESG data, investor behavior, and market outcomes across sectors. Methods like regression, panel modeling, and cross-market comparison can assess its validity. Incorporating sentiment analysis, deep learning, or time-series models into policy text analysis may also enhance insights into ESG discourse and stakeholder responses.

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