Differentiated Internationalization Effects of ESG Dimensions: Divergent Mechanisms of Environmental, Social, and Governance Factors

Jianing Li
School of International Trade and Economics, Shandong University of Finance and Economics, jinan, 250002, China
3250319805@qq.com

ABSTRACT

ESG is often treated as a composite signal of firm responsibility, yet internationalization exposes firms to different regulatory, stakeholder, and contracting conditions across host countries. This paper reviews how the environmental, social, and governance dimensions of ESG generate differentiated internationalization effects. It argues that environmental performance mainly works through regulatory fit and green capability transfer. The social dimension works through stakeholder trust, labor responsibility, community acceptance, and local embeddedness, but its effects are more culturally contingent. Governance works through transparency, agency-risk reduction, investor protection, and cross-border contracting credibility. These mechanisms can reinforce one another, but they are not interchangeable. The paper proposes a differentiated ESG-internationalization framework linking each dimension to specific mechanisms, boundary conditions, and entry-mode implications.

Keywords: ESG; Internationalization; Environmental performance; Social responsibility; Corporate governance

1. INTRODUCTION

ESG has become a central language through which firms present responsibility and long-term value to investors, regulators, customers, and communities. Yet its internationalization effects remain under-specified when ESG is treated as one aggregate score. A composite score may help comparison, but it can hide the fact that environmental, social, and governance practices operate through different mechanisms. Reviews of ESG and CSR research emphasize the breadth of constructs covered by these labels [1], making a dimension-level approach necessary for explaining foreign expansion.

Internationalization is especially suitable for such differentiation. Foreign entry exposes firms to new legal rules, stakeholder expectations, disclosure regimes, cultural norms, and investor scrutiny. ESG disclosure has been linked with firm internationalization and financial performance in recent Asia-Pacific evidence [2], but this relationship does not show that all ESG dimensions matter in the same way. Carbon-management capabilities may matter in climate-sensitive markets, board governance may matter for investors, and social responsibility may matter where labor or community standards are salient.

This paper argues that ESG affects internationalization through three mechanisms. Environmental performance influences regulatory fit and green competitive advantage. Social responsibility influences stakeholder embeddedness and local acceptance. Governance quality influences transparency, contracting credibility, and agency-risk reduction. The contribution is to shift from aggregate ESG logic to a mechanism-based framework explaining when each dimension supports, constrains, or conditions international expansion.

2. ESG AND INTERNATIONALIZATION: CONCEPTUAL FOUNDATIONS

2.1 From Aggregate ESG Scores to Dimension-Specific Effects

Aggregate ESG scores are convenient but analytically blunt. They combine indicators that differ in time horizon, stakeholder audience, materiality, and observability. Environmental indicators often concern emissions, resource use, or green innovation. Social indicators cover labor standards, human rights, customer responsibility, and community relations. Governance indicators concern board structure, transparency, shareholder rights, corruption control, and incentives.

Treating these dimensions as substitutes can mislead internationalization analysis because the same score may reflect very different capability profiles.

This distinction matters because internationalization converts ESG from a domestic reputation signal into a cross-border screening device. Host-country regulators may read the environmental dimension as evidence of compliance readiness, local communities may read the social dimension as evidence of respect and reciprocity, and investors may read the governance dimension as evidence of monitoring quality. A firm may therefore appear strong on ESG in aggregate while still lacking the specific dimension required by a target market.

2.2 Internationalization as a Legitimacy and Capability Process

Internationalization is not only geographic expansion; it is a process of overcoming unfamiliarity, coordination costs, and legitimacy deficits. The liability of foreignness framework [3] explains why foreign firms face additional costs relative to local competitors, including weaker local embeddedness. ESG can reduce some of these costs when it signals reliability or creates transferable capabilities, but it can also increase exposure when stakeholders challenge public commitments. The key question is which ESG dimension reduces which foreignness cost under which host-market condition.

2.3 Institutional Distance and Stakeholder Pressure

Host-country institutions condition ESG effects because firms must satisfy different rules and expectations across markets. Multinational enterprises face legitimacy challenges under institutional complexity [4], and ESG adds environmental regulation, labor norms, community standards, and governance expectations to this process. Institutional distance can make a home-country ESG practice less credible or less relevant abroad. Thus, ESG affects internationalization through host-country interpretation, not only through firm-level performance.

Institutional distance also changes the cost of learning. When the host market differs sharply from the home market, firms must learn not only formal rules but also which ESG concerns become politically salient, which disclosures are trusted, and which local actors can challenge the firm’s legitimacy. This is why the same ESG practice can operate as a capability in one market and as an incomplete signal in another.

3. ENVIRONMENTAL DIMENSION: REGULATION, CAPABILITY, AND GREEN LEGITIMACY

3.1 Environmental Compliance and Host-Country Regulatory Fit

The environmental dimension influences internationalization first through regulatory fit. Firms entering markets with strict pollution rules, carbon pricing, or disclosure requirements may benefit from prior environmental capabilities because compliance costs and legitimacy barriers are lower. Ecological responsiveness research shows that firms go green for competitiveness, legitimation, and ecological responsibility motives [5], and these motives are relevant to foreign entry. Credible environmental routines can position a firm as compatible with host-country policy priorities.

3.2 Green Innovation and Transferable Competitive Advantage

Environmental performance can support internationalization when it reflects transferable green capabilities rather than symbolic reporting. The natural-resource-based view treats pollution prevention, product stewardship, and sustainable development as strategic capabilities [6]. In international markets, such capabilities may support energy-efficient products, low-carbon supply chains, and partnerships with demanding buyers. Environmental strength is therefore not only a legitimacy signal; it can be a competitive resource when it fits host-country infrastructure and demand.

3.3 Boundary Conditions: Greenwashing and Policy Volatility

Environmental advantages are fragile when disclosure credibility is weak. Greenwashing research identifies gaps between environmental communication and substantive performance [7], which can be risky in foreign markets where stakeholders may already distrust outsider firms. Policy volatility adds another boundary condition: firms may invest around one regulatory regime and then face changed subsidies, reporting standards, or climate priorities. Environmental ESG can reduce regulatory friction when credible, but increase exposure when claims outrun capability.

The environmental dimension is therefore most useful for internationalization when it is embedded in operating routines rather than limited to reporting language. Firms need auditable metrics, supplier controls, product-level evidence, and adaptation plans for host-country regulation. Otherwise, environmental claims may attract attention without providing the operational capacity needed to survive scrutiny.

4. SOCIAL DIMENSION: STAKEHOLDER TRUST AND LOCAL EMBEDDEDNESS

4.1 Labor, Human Rights, and Supply-Chain Responsibility

The social dimension affects internationalization through stakeholder trust and operational legitimacy. Labor practices, human rights, safety, customer responsibility, and supply-chain standards shape whether host-country stakeholders view a foreign firm as acceptable. Institutional theory of corporate social responsibility suggests that firms behave responsibly under specific regulatory, normative, and stakeholder conditions [8]. In internationalization, these conditions vary strongly across countries, especially when labor standards, supplier monitoring, or community consultation are visible.

4.2 Community Acceptance and Consumer Legitimacy

Social responsibility also affects market entry through local embeddedness. Foreign firms need employees, distributors, suppliers, regulators, consumers, and community actors to accept their presence. Stakeholder salience theory [9] explains why some social issues become urgent in particular host markets: stakeholders differ in power, legitimacy, and urgency. A community affected by land use, a union concerned with work conditions, or consumers sensitive to data protection may become decisive. Social ESG therefore requires local diagnosis, not only global templates.

4.3 Cultural Contingency of Social Expectations

The social dimension is highly culturally contingent because it depends on local norms about fairness, employment, community obligation, gender, privacy, and consumer protection. Recent evidence from Chinese multinational enterprises shows that internal and external CSR can influence internationalization speed [10], but the direction and strength of such effects should be interpreted through context. Social responsibility can accelerate entry when it builds trust, but slow expansion when host-country expectations require deeper adaptation.

This contingency makes the social dimension less portable than environmental technology or governance routines. A labor policy can be written globally, but its acceptance depends on local wage norms, worker voice, supplier dependence, and community memory of foreign firms. Social ESG therefore requires mechanisms for listening and adjustment, not only compliance checklists.

5. GOVERNANCE DIMENSION: TRANSPARENCY, CONTRACTING, AND INVESTOR CONFIDENCE

5.1 Governance Quality and Cross-Border Credibility

Governance affects internationalization by reducing agency risk and increasing credibility with investors, lenders, partners, and regulators. Strong governance systems help external actors evaluate whether managers will honor commitments, disclose risks, and protect stakeholders. Investor-protection research links governance institutions with the control of agency problems [11], and this logic travels into firm internationalization. When foreign partners have limited information about internal controls, governance quality can reduce perceived cooperation risk.

5.2 Disclosure, Anti-Corruption, and Institutional Trust

Governance also matters because foreign entry requires interaction with public authorities, local partners, and capital markets. Transparent disclosure, anti-corruption controls, independent boards, and reliable audits help firms navigate scrutiny. Research on corporate governance and international location decisions of multinational enterprises [12] supports the view that governance is relevant to where firms expand, not merely how they are financed. Governance can affect market selection by shaping which environments a firm can credibly enter.

5.3 Governance as a Moderator of Environmental and Social Signals

Governance is both a direct internationalization factor and a credibility condition for the other ESG dimensions. Environmental and social claims are more persuasive when the firm has disclosure controls, board oversight, and accountability mechanisms. Without governance, environmental performance may be read as greenwashing and social commitments as public relations. This moderating role explains why ESG dimensions are interdependent but not interchangeable: governance helps stakeholders decide whether to trust environmental and social claims.

Governance also determines how quickly a firm can correct ESG failures after entry. Foreign expansion increases coordination complexity across subsidiaries, suppliers, advisors, and joint-venture partners. Clear reporting lines, audit rights, whistleblowing channels, and board-level risk oversight make ESG commitments enforceable across distance. In this sense, governance is the infrastructure that turns environmental and social promises into controllable organizational practices.

6. A DIFFERENTIATED ESG-INTERNATIONALIZATION FRAMEWORK

6.1 Three Mechanisms: Regulatory Fit, Stakeholder Embeddedness, and Contracting Credibility

The differentiated framework links each ESG dimension to a primary mechanism. Environmental performance creates regulatory fit and green capability transfer. Social responsibility creates stakeholder embeddedness and local acceptance. Governance quality creates contracting credibility and investor confidence. Multinational firms must orchestrate responsibility across countries rather than impose one uniform template [13], so these mechanisms should be diagnosed separately before foreign entry. Environmental strength matters most in climate-sensitive sectors, social strength where local legitimacy is contested, and governance strength where information asymmetry is high.

6.2 Complementarity and Substitution Among ESG Dimensions

The ESG dimensions can complement one another. Strong governance can make environmental and social claims more credible; environmental capability can make community-health promises more plausible; social embeddedness can help firms interpret local environmental concerns. Yet substitution is limited. A strong environmental profile cannot fully compensate for weak governance if investors fear corruption. Strong governance cannot fully compensate for poor labor practices if communities mobilize against the firm. Dimensions reinforce one another when all meet minimum credibility thresholds, but weaknesses can become binding constraints.

6.3 Entry Mode, Market Selection, and Performance Implications

Different ESG profiles imply different internationalization choices. Firms with strong environmental capabilities may prefer markets with strict green regulation or buyers that reward low-carbon products. Firms with strong social capabilities may use alliances or gradual entry modes that allow local embeddedness. Firms with strong governance may have advantages in acquisitions, financing, and complex contracting. Evidence on ESG scores, financial performance, and geographic international diversification in Multilatinas [14] supports the broader claim that ESG and international diversification are strategically connected, although dimension-specific pathways need testing.

These implications can be translated into managerial and research priorities. Managers should ask which internationalization friction each ESG strength reduces before choosing host markets and entry modes. Researchers should test whether environmental performance predicts entry into stricter regulatory markets, whether social performance predicts alliance stability or local acceptance, and whether governance quality predicts acquisition success or financing terms. Supply-chain internationalization is another priority because firms may internationalize through suppliers and buyers without owning foreign subsidiaries.

7. CONCLUSION

ESG affects internationalization through differentiated mechanisms. Environmental performance shapes regulatory fit and green capability transfer. Social responsibility shapes stakeholder trust and local embeddedness. Governance quality shapes transparency, contracting credibility, and the trustworthiness of environmental and social claims. These dimensions can reinforce one another, but they cannot be collapsed into a single reputation score without losing explanatory power. Firms should design internationalization strategy around the ESG mechanism that matters in the target market, while researchers should move toward mechanism-based, dimension-specific analysis.

REFERENCES

[1] Gillan, S. L., Koch, A., & Starks, L. T. (2021). Firms and social responsibility: A review of ESG and CSR research in corporate finance. Journal of Corporate Finance, 66, 101889.

[2] Hussain, W., Ong, T. S., Kamarudin, F. B., Khan, M. A., & Bács, Z. (2024). ESG disclosure, firm internationalization, and firm financial performance: Evidence from Asia-Pacific. Journal of International Studies, 17(2), 240-261.

[3] Zaheer, S. (1995). Overcoming the liability of foreignness. Academy of Management Journal, 38(2), 341-363.
[4] Kostova, T., & Zaheer, S. (1999). Organizational legitimacy under conditions of complexity: The case of the multinational enterprise. Academy of Management Review, 24(1), 64-81.
[5] Bansal, P., & Roth, K. (2000). Why companies go green: A model of ecological responsiveness. Academy of Management Journal, 43(4), 717-736.
[6] Hart, S. L. (1995). A natural-resource-based view of the firm. Academy of Management Review, 20(4), 986-1014.
[7] Delmas, M. A., & Burbano, V. C. (2011). The drivers of greenwashing. California Management Review, 54(1), 64-87.
[8] Campbell, J. L. (2007). Why would corporations behave in socially responsible ways? An institutional theory of corporate social responsibility. Academy of Management Review, 32(3), 946-967.
[9] Mitchell, R. K., Agle, B. R., & Wood, D. J. (1997). Toward a theory of stakeholder identification and salience: Defining the principle of who and what really counts. Academy of Management Review, 22(4), 853-886.
[10] Guo, Z., & Xie, Y. (2025). Impact of internal and external corporate social responsibility on internationalization speed: Evidence from Chinese multinational enterprises. Corporate Social Responsibility and Environmental Management, 32(1), 481-505.
[11] La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. (2000). Investor protection and corporate governance. Journal of Financial Economics, 58(1-2), 3-27.
[12] Dam, L., Scholtens, B., & Sterken, E. (2007). Corporate governance and international location decisions of multinational enterprises. Corporate Governance: An International Review, 15(6), 1330-1347.
[13] Asmussen, C. G., & Fosfuri, A. (2019). Orchestrating corporate social responsibility in the multinational enterprise. Strategic Management Journal, 40(6), 894-916.
[14] Duque-Grisales, E., & Aguilera-Caracuel, J. (2021). Environmental, social and governance (ESG) scores and financial performance of Multilatinas: Moderating effects of geographic international diversification and financial slack. Journal of Business Ethics, 168(2), 315-334.