ESG Controversy Deterioration and the Cost of Corporate Bond Financing

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ABSTRACT

This paper examines whether deterioration in a firm's ESG controversy profile affects the cost of corporate bond financing. Existing studies have mainly examined whether firms with stronger ESG performance or fewer ESG controversies enjoy lower borrowing costs. This paper takes a different perspective by focusing on changes in controversy-related ESG risk and by examining the primary bond market, where firms raise new debt and where financing costs are directly observed. The study uses annual firm-level ESG controversy data matched with corporate bond issuance records. ESG controversy deterioration is measured using changes in ESG Controversies Scores, increases in controversy counts and the emergence of new controversy indicators across environmental, social and governance categories. These measures are lagged and matched with subsequent bond issues to reduce timing concerns and to ensure that the ESG information used in the analysis is available before the financing decision. The dependent variable in the main bond-level analysis is the corporate bond issuance spread. Where available, this is measured using the reported issue spread; otherwise, it can be constructed as the difference between the offering yield and the relevant risk-free benchmark yield. The empirical model controls for standard bond characteristics, including maturity, issue size, seniority, coupon structure and credit rating at issuance.

JEL Codes:

Keywords: *ESG controversy deterioration, Corporate Finance, Corporate Bond Financing.*