***ASSOCIAÇÃO DE POLITÉCNICOS DO NORTE* (APNOR)**
INSTITUTO POLITÉCNICO DE BRAGANÇA

The Impact of ESG Scores on Dividend: Evidence from Euronext-Listed Companies

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***Bragança*, December 2025.**

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Abstract

This study investigates the relationship between Environmental, Social, and Governance (ESG) performance and dividend payout policies among European firms listed on Euronext. The primary objective is to determine whether firms with higher ESG scores are more likely to distribute dividends. Based on a database of companies from Euronext stock exchange countries, our results reveal a positive and statistically significant association between overall ESG scores and dividend payout ratios. Among the three ESG dimensions, Governance exerts the strongest positive influence, followed by Environmental and Social scores. The relationship is less consistent when dividend yield is considered as the dependent variable. Additionally, insider ownership and board independence positively correlate with higher dividend payouts, while greater outside ownership is negatively related. These findings indicate that firms with superior ESG performance and robust governance structures tend to adopt more shareholder-friendly dividend policies, reflecting a commitment to rewarding shareholders and maintaining investor confidence. This suggests that ESG considerations are increasingly integrated into corporate and policymaker interest in sustainable business practices within the European market.

Keywords: ESG, Dividend(payout), Dividend Yield, Sustainability, Governance, Euronext Firms

Resumo

Este estudo investiga a relação entre o desempenho Ambiental, Social e de Governança (ESG) e as políticas de distribuição de dividendos entre as empresas europeias listadas na Euronext. O objetivo principal é determinar se as empresas com pontuações mais altas de ESG são mais propensas a distribuir dividendos, utilizando a razão de pagamento de dividendos (dividendos sobre ativos totais). Com base em um banco de dados de empresas de países da bolsa de valores Euronext, nossos resultados revelam uma associação positiva e estatisticamente significativa entre as pontuações gerais de ESG e as razões de pagamento de dividendos. Entre as três dimensões do ESG, a Governança exerce a influência positiva mais forte, seguida pelas pontuações Ambiental e Social. A relação é menos consistente quando o rendimento de dividendos é considerado como variável dependente. Além disso, a posse interna e a independência do conselho estão positivamente correlacionadas com maiores pagamentos de dividendos, enquanto a maior posse externa está negativamente relacionada. Esses resultados indicam que as empresas com desempenho superior em ESG e estruturas de governança robustas tendem a adotar políticas de dividendos mais favoráveis aos acionistas, refletindo um compromisso em recompensar os acionistas e manter a confiança dos investidores. Isso sugere que as considerações ESG estão cada vez mais integradas nas práticas corporativas e nas políticas públicas voltadas para práticas de negócios sustentáveis no mercado europeu.

Palavras-chave: ESG, Distribuição de Dividendos, Rendimento de Dividendos, Sustentabilidade, Empresas Euronext, Análise de Dados em

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Abbreviations

CEO: Chief Executive Officer

CFP: Corporate Financial Performance

CG : Corporate Governance

CSR: Corporate Social Responsibility

ESG: Environmental, Social and Governance

LSEG: London Stock Exchange Group

MiFID: Markets in Financial Instruments Directive

OLS: Ordinary Least Squares

PRI: Principles for Responsible Investment

SFDR: Sustainable Finance Disclosure Regulation

SRI: Socially Responsible Investing

UE: European Union

UK: United Kingdoms

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Introduction

Regulatory and financial sectors are increasingly integrating ESG metrics into mainstream business practices. For instance, MiFID II and SFDR require financial advisors to discuss ESG factors with clients before recommending investments, underscoring the growing importance of ESG in capital allocation. Creditors and equity investors also view ESG scores as indicators of firm-level risk, assuming that lower ESG ratings correlate with a higher default probability (Apergis, Poufinas & Antonopoulos, 2022). Investor time horizons further influence ESG preferences: long-term investors favor firms with strong ESG engagement for sustainable value creation, whereas short-term investors may view ESG expenditures as a cost that reduces immediate returns (Zahid, Taran, Khan & Chersan, 2023; Uyara, Wasiuzzaman, Kuzey & Karamand, 2024).

Despite growing interest in ESG performance, empirical evidence on its relationship with dividend policy remains inconclusive. Some studies argue that firms with high ESG investment are associated with greater profitability, lower perceived risk (Aydoğmuş, Gülay & Ergun, 2022; He, Liu, & Chen, 2023), and lower costs of capital and debt (Ernst & Woithe, 2024; Apergis, Poufinas & Antonopoulos, 2022). These firms can provide more stable and generous dividends (e.g., Bilyay-Erdogan, Ozturk Danisman & Demir, 2023; Salvi, Nirino, Battisti & Gianfrancesco, 2024; Zhou & Bu, 2025). High ESG performers may also sustain dividend distributions as a signaling mechanism to affirm their financial health, bolster investor confidence, and enhance their corporate reputation (Kräussl, Oladiran & Stefanova, 2024; Benlemlih, 2019). From a stakeholder theory perspective, ESG investment is viewed as an approach that balances the interests of shareholders and broader stakeholders (Mitchell, Agle & Wood, 1997), thereby supporting the alignment of sustainability practices with long-term shareholder wealth.

However, other researchers point to a potential trade-off between ESG engagement and dividend distribution. ESG initiatives often require substantial internal funding, prompting firms to retain earnings that might otherwise be distributed as dividends (Salman, Djunaedi & Ardianto, 2024). In some cases, particularly with weak governance, managerial discretion over ESG spending may lead to misallocation of resources that do not maximize shareholder value, ultimately reducing dividends (Zhou & Bu, 2025; Saeed & Zamir, 2021). Thus, while ESG may reflect a firm's commitment to sustainability, it may also limit immediate shareholder returns, particularly where ESG spending competes with capital available for payouts. As a result, theoretical and empirical literature provide mixed conclusions about whether ESG investment has a positive, negative, or neutral effect on dividend policy.

The objective of this study is to determine whether ESG scores have a significant impact on corporate dividend payout. Additionally, the study aims to assess how the three components of ESG - Environmental, Social, and Governance - individually affect dividend behavior. Furthermore, we investigate whether ESG performance affects dividend yield, which reflects market-based

shareholder returns. This study also examines how governance characteristics, including ownership structure and board composition, may impact the ESG–dividend relationship.

The main research question is: Does ESG performance have a significant effect on corporate dividend policy? To address this question, a quantitative methodology is employed, based on panel data covering publicly listed firms from various European countries from 2019 to 2023. Multiple regression models (OLS) are used to test the impact of ESG scores and components on dividend behavior. Robustness checks, including the use of dividend yield and consideration of firm-specific governance factors, are incorporated. Europe is selected as the research context due to the region's advanced ESG regulatory framework and the relative scarcity of studies exploring ESG–dividend dynamics in European markets. Our findings suggest that ESG-oriented firms may adopt more shareholder-aligned and financially disciplined dividend policies.

This study provides robust evidence that ESG performance has a positive impact on dividend payouts in Euronext-listed European firms, a context that has been underexplored in ESG–dividend research. Unlike previous studies, it distinguishes between Div/TA and dividend yield, showing that ESG enhances internal financial capacity rather than relying on market-driven measures. Furthermore, it demonstrates that ownership structure and board size act as key channels through which ESG translates into higher dividends, highlighting the essential role of governance mechanisms—an aspect largely overlooked in earlier work (Benlemlih, 2019; Krieger & Mauck, 2024; Bilyay-Erdogan, Ozturk Danisman & Demir, 2023; Salvi, Nirino, Battisti & Gianfrancesco, 2024. Among others).

This dissertation is structured as follows. The next section reviews literature on sustainability, dividend policy, stakeholder theory, and determinants of dividend decisions to establish the theoretical background. The research methodology is then presented, including data sources, sample selection, hypothesis development, and the econometric models employed. Section three presents and analyzes empirical results, examining the relationship between ESG scores and dividend behavior. The final section summarizes the key findings, discusses the practical and policy implications, and suggests avenues for future research.

1. Theoretical background

This chapter provides an overview of key concepts and previous research related to sustainability, dividend policies, stakeholder perspectives, and factors influencing dividend decisions

1.1 Sustainability

This section explores the evolving role of sustainability in corporate decision-making, with a focus on the Environmental, Social, and Governance (ESG) considerations. It begins by distinguishing ESG from the broader concept of Corporate Social Responsibility (CSR), followed by a discussion on ESG disclosures and ratings, and their significance for investors and stakeholders. Finally, it examines the impact of sustainability performance on overall corporate performance, highlighting both financial and reputational implications.

The Green Book of the European Commission (Promoting a European Framework for Corporate Social Responsibility - Green Paper) gave an approach to CSR: "Where corporate social responsibility is a process by which companies manage their relationships with a variety of stakeholders who can have a real influence on their license to operate". An Extended definition asserts that corporate social responsibility is the responsibility of an organization for the impact of its decisions and actions on society and the environment through transparent and ethical behavior in key areas, such as organizational governance, human rights, work practices, the environment, fair operational practices, consumer issues, social involvement, and development of the local community" (PN-EN ISO 26000:2021-04, p. 3). According to Kaźmierczak (2022), CSR reflects the need for organizations to balance profits with sustainable socio-economic development and the improvement of the quality of life in the community in which they operate.

A dynamic evolution marked by a shift from CSR as an integral part of modern business practices to an acronym that represents Environmental – E, Social – S, and Governance – G. The ESG set of non-financial performance indicators, also known as sustainable or socially responsible investing is an investment strategy (Kartal, Taşkın, Kılıç Depren & Pata, 2024) intended to ensure the responsibility of the organization and may be subject to assessment by investors and other stakeholders (Kaźmierczak, 2022).

ESG covers topics such as energy efficiencies, carbon footprints, greenhouse, gas emissions, biodiversity, waste management, labor standards, workplace diversity, human rights, talent management, community relations, privacy, and health and safety, as well as governance factors like board composition, sustainability oversight, executive compensation, political contributions, lobbying, and corruption (Bergman, Deckelbaum & Karp, 2020).

The CSR is a general sustainability framework primarily used by companies, whereas ESG is a measurable sustainability assessment, more popular with investors.

Table 1. Key Differences Between CSR and ESG

	CSR	ESG
Measurability	Hard to measure objectively, it leans toward quality.	Highly measurable and quantifiable, leans toward Quantity.
Usefulness	To reach internal goals, including achieving greater social responsibility and developing healthy, sustainable workplace cultures	To gain the measurable proof they need regarding the effectiveness of these efforts
Communication	help better communicate its values to its employees and stakeholders, fostering a better work environment and potential for recognizable community outreach.	Help a company prove to current and potential investors that its efforts in social, environmental, and governance responsibility are paying off.

Source: Author`s own elaboration based on Kaźmierczak (2022, p. 283)

1.1.2 ESG Disclosure and ESG Scores

In recent years, ESG ratings have emerged as key tools for assessing corporate sustainability (Postiglione, Carini & Falini, 2024). These ratings provide a standardized, quantitative framework to evaluate a company's environmental, social, and governance performance, often regarded as the best instruments available for measuring corporate sustainability (Kaźmierczak, 2022). ESG ratings serve multiple purposes beyond ethical investment screening—they are also widely used for risk assessment, strategic planning, and guiding investor decision-making.

ESG ratings rely heavily on corporate disclosures, which refer to the voluntary or mandatory communication of environmental, social, and governance practices through public documents, such as annual reports and sustainability reports (Kartal, Taşkın, Kılıç Depren & Pata, 2024). These disclosures play a critical role in informing a broad range of stakeholders—including investors, customers, employees, suppliers, regulators, and society at large—about a company's sustainability-related policies and performance (Moussa & Elmarzouky, 2023).

Environmental disclosures typically include data on a firm's carbon footprint, waste management, pollution control, and energy and water consumption. Social disclosures cover labor practices, human rights policies, employee well-being, and diversity initiatives. Governance disclosures encompass information regarding board composition, shareholder rights, ethical business conduct, and regulatory compliance (Kartal, Taşkın, Kılıç Depren & Pata, 2024).

Companies that provide more extensive ESG disclosures tend to receive higher ESG scores, as rating agencies and regulators use this information to calculate these scores (Kartal, Taşkın, Kılıç Depren & Pata, 2024). Most investors, lacking the time or expertise to analyze complex sustainability data themselves, rely on these ESG scores as simplified indicators of a firm's ESG performance (Kartal, Taşkın, Kılıç Depren & Pata, 2024).

However, despite their usefulness, ESG ratings face significant challenges. A major concern is the inconsistency among rating agencies, which often apply differing criteria and employ opaque methodologies, resulting in divergent evaluations of the same company (Gibson, Krueger & Schmidt, 2021). This lack of standardization undermines the credibility of ESG ratings and creates confusion among investors and financial analysts. Furthermore, the absence of regulatory oversight exacerbates these issues. These inconsistencies have real financial consequences. According to (Postiglione, Carini & Falini, 2024), disagreement among ESG ratings increases the perceived risk of a firm, thereby raising its cost of capital. An increase in the cost of capital reduces a company's intrinsic value and can negatively impact financial decisions, such as dividend payouts. Consequently, even companies with strong sustainability performance may be penalized due to flawed or inconsistent ESG assessments driven by rating agencies' perceptions.

1.1.3 The impact of Sustainability on corporate performance: a balanced perspective

Previous research has provided two competing empirical studies to describe the impact of ESG on various aspects of firm performance, encompassing both value-creating and value-destroying effects. These studies encompass both financial outcomes, such as profitability and capital costs, as well as intangible factors like reputation, governance, and stakeholder trust.

The impact of ESG on a firm's intangible assets as an investment has been widely recognized. High levels of ESG performance enhance a company's reputation across various dimensions, including social welfare, ecological responsibility, employee satisfaction, and product or service quality. This, in turn, allows firms to differentiate themselves in the marketplace (He, Liu & Chen, 2023). Drawing on signaling theory, ESG practices are viewed as indicators of corporate resilience, long-term strategic vision, and operational transparency (Friske, Hoelscher & Nikolov, 2023). Furthermore, (Friske, Hoelscher & Nikolov, 2023) argue that corporations disclose ESG-related information not only to reduce information asymmetry but also to signal their commitment to social and environmental responsibility, thereby reinforcing stakeholder trust - an intersection of both signaling and stakeholder theories. Stakeholders, including shareholders, increasingly rely on ESG scores to evaluate corporate performance, often interpreting these scores as proxies for strong managerial competence (Kartal, Taşkın, Kılıç Depren & Pata, 2024).

ESG performance enhances firm valuation by building investor confidence and earning greater trust from stakeholders, leading to initiatives such as resource efficiency, inclusive employment, and robust governance (Kräussl, Oladiran, & Stefanova, 2024). This, in turn, reduces reliance on internal resources (He, Liu, & Chen, 2023). From a risk perspective, firms with a high degree of social responsibility may experience lower financial risk due to more stable relationships with governments and the financial community (Farre-Mensa, Michaely & Schmalz, 2014). Moreover, in financing, firms with high SR can replace costly explicit obligations with less expensive implicit ones, benefiting from lower costs of equity financing and mitigating event risks, and maintain lower levels of total debt (Apergis, Poufinas & Antonopoulos, 2022; Chen, Li, Zeng & Zhu, 2023; Yang, Tang, Hu & Yao, 2025).

(Kartal, Taşkın, Kılıç, Depren & Pata, 2024) argue that companies with high ESG scores exhibit greater resilience during economic instability. Additionally, high ESG performance acts as an effective corporate governance mechanism, reducing risks and addressing agency problems (Yang, Tang, Hu & Yao, 2025).

In contrast, another view predicts that companies engaged in SR lose focus on profitability and instead pursue pleasing stakeholders at the expense of shareholders. suggesting a negative relationship when resources are channeled towards less profitable sustainable activities (Yang, Tang, Hu & Yao, 2025).

1.2 Corporate payout policy: Dividends

This section discusses key theories of dividends, such as signaling, agency, and life-cycle models. The section also reviews recent studies linking ESG and CSR practices to dividend behavior.

1.2.1 Dividend Theories

Over the years, several theories have been proposed to explain the concept of dividends. Many papers have tried to provide rational explanations for why firms distribute dividends and why investors like them. (Miller & Modigliani, 1961) introduced the dividend irrelevance theory. Subsequent theories have refined this perspective, proposing a range of theories about dividend relevance, including signaling theory and agency theory (Allen & Michaely, 1995; Bhattacharya, 1979), which provide excellent reviews of these theories and the related empirical facts.

Miller and Modigliani conclude that “no matter how the pie is divided, it is important that it exists” (as cited in Livoreka, Hetemi, Shala, Hoti & Asllanaj, 2014, p 392). They argue that the value of a corporation depends solely on the profits generated from its investment activities, rather than on the degree of risk or the manner in which retained earnings are distributed as dividends. (Black,1976) argues that “The harder we look at the dividend picture, the more it seems like a puzzle, with pieces that just don’t fit together”.

The irrelevance proposition by Miller & Modigliani (1961) argues that in perfect and complete capital markets (no taxes, symmetric information, complete contracting possibilities, no transaction costs), the only determinant of a firm’s value is the present value of what the firm produces, which is a function of its investment policy, not its payout policy. Second, manipulations of the right-hand side of the balance sheet have no effect on a firm’s value. As a result, once an investment is chosen to maximize firm value, how much the firm pays out will not affect its value. Net payout can be thought of as the residual cash flow, after investment decisions have been made. Third, from the perspective of investors, dividend policy is irrelevant because any desired stream of payments can be replicated by appropriate purchases and sales of equity. Given the ‘perfect world’ assumptions behind M&M, a firm can pay a dividend that is simply the residual, it can pay a large dividend financed by (costless) external finance, or pay nothing and accumulate the money in the firm (Miller & Modigliani,1961)

seminal paper demonstrates that capital gains and dividends are substitutes for each other. Additionally, investors could generate their own “home-made dividends” by selling stock if they chose to do so. However, in the real world with market imperfections such as taxes, transaction costs, asymmetric information, and principal-agent conflict, dividend policy has been shown to affect shareholders' value.

Dividend-signaling theory: In contrast to the dividend irrelevance theory proposed by Miller and Modigliani (1961), the dividend-signaling theory emphasizes the role of information asymmetry between managers and investors. When managers possess private information about the firm’s future performance, dividend payments can serve as an effective mechanism to reduce this asymmetry. Firms experiencing high levels of information asymmetry are therefore more likely to distribute dividends as a means of conveying information and signaling financial strength to external investors. By increasing or maintaining stable dividend payments, managers can demonstrate confidence in the firm’s future earnings prospects and reduce uncertainty among capital providers (Bhattacharya, 1979). This makes dividend decisions particularly sensitive: once dividends are set, it becomes difficult to adjust them without potentially damaging investor confidence, which is costly to reverse. In fact, reducing or omitting dividends can be interpreted as a signal of trouble, leading to negative reactions from investors and a decline in stock prices. Therefore, firms with high information asymmetry are more likely to maintain or even increase dividends. Investor reactions are typically positive when dividends are initiated or increased, while omissions tend to provoke sharp negative responses, underlining the strong connection between dividends and earnings (Bhattacharya, 1979). A dividend typically reflects good governance and predictable financial health (Yang, Tang, Hu & Yao, 2025). Thus, companies that maintain or increase dividends demonstrate their financial robustness and the dependability of future cash flows. This openness enhances investor confidence and increases market value, ultimately benefiting shareholder wealth (Farre-Mensa, Michaely & Schmalz, 2014; Zhou & Bu, 2025).

The second proposal suggests that investors exert pressure on firms to pay them, as they are traditionally used as a valuation tool (Bhattacharya, 1979). According to signaling theories, dividend distribution serves as a signaling device for the management’s quality and commitment level, signaling that increases in payout will be followed by improvements in operating performance (Bhattacharya, 1979). Second, there is no formal signaling model that explores the implication that dividends signal not only the expected level of cash flow but also the riskiness of the cash flow (Anand, 2004), as they provide a signaling mechanism for the future prospects and thus affect their market value. If the good news in a dividend increase is not about increases in future cash flow (per empirical evidence), then it might concern a decline in (systematic) risk exposure of these cash flows (Farre-Mensa, Michaely & Schmalz, 2014).

Agency theory: This theory diverges from the assumptions of the Modigliani-Miller theorem by acknowledging one of the significant market imperfections: Conflicts of interest. Agency theory explains dividend decisions in principal-agent problems, where conflicts of interest (Jensen, 1986) can arise between managers and shareholders, as well as between large and small stakeholders.

According to agency theory, these conflicts may significantly affect payout policy, the persistent distribution of cash out of the firm disciplines managers and reduces the extent of agency costs (e.g., Easterbrook, 1984). In this context, a high payout ratio may induce management to be more disciplined in the use of the firm's resources to prevent self-interested managers from investing excess cash in negative NPV projects or obtaining private benefits (Farre-Mensa, Michaely & Schmalz, 2014).

Lintner made several important observations regarding dividend policies. Allen & Michaely (1995) argue that Managers believe the market puts a premium on firms with a stable dividend policy. First firms are primarily concerned with the stability of dividends. They do not set dividends de novo each quarter. Instead, they first consider whether any change from the existing rate is necessary. Only when they have decided a change is necessary do they consider how large it should be. Lintner's second argument is that dividend policy was set first, with other policies adjusted afterward. If a firm had many investment opportunities and insufficient internal funds, it would resort to raising external capital.

The life-cycle theory takes a more practical view. It suggests that firms at different stages of their life cycle generate different levels of free cash flow, which in turn influences their ability and decision to pay dividends. Growing firms typically have low free cash flow because they reinvest heavily in new projects, leading to lower or no dividends. In contrast, mature firms often generate high free cash flow due to fewer investment opportunities, making it easier for them to distribute dividends. This link between a firm's stage, its free cash flow, and dividend payments suggests that dividend policy is relevant and carries information, thereby challenging the assumptions of dividend irrelevance in real-world conditions (DeAngelo, DeAngelo & Stulz, 2006).

The catering theory highlights that dividend policies are flexible tools managers use to align with current investor preferences, making dividends a meaningful factor in stock valuation. Baker and Wurgler (2004) argue that catering theory is based on three key ideas. First, it identifies a group of uninformed investors who prefer firms that pay cash dividends, creating demand for these stocks. Second, due to limits on arbitrage—such as trading costs and market inefficiencies—this demand can influence current share prices, resulting in a "dividend premium", or a price difference between dividend payers and non-payers. Third, managers respond rationally to this situation by weighing the short-term benefits of catering to investor preferences against the long-term costs of changing dividend policies. Essentially, managers "give investors what they currently want": they tend to initiate or increase dividends when dividend-paying firms are valued more highly and omit or reduce dividends when investors prefer nonpayers.

1.2.2 Related Studies

Recent research has increasingly focused on the relationship between ESG performance and corporate dividend policy, highlighting how sustainability practices intersect with shareholder returns. For instance, Matos, Barros & Sarmento (2020) find that more sustainable firms within the STOXX Europe 600 from 2000 to 2019 exhibit more stable dividend payouts, with environmental and

governance pillars particularly driving this stability. Similarly, Bilyay-Erdogan, Ozturk, Danisman & Demir (2023) demonstrate that ESG performance enhances dividend distributions in European firms from 2002 to 2019 through both earnings and risk channels, with results that are robust to alternative specifications. From 1991 to 2016, in the U.S. context, Krieger & Mauck (2024) demonstrate a positive relationship between ESG commitments and dividend payer status, revealing that firms with stronger ESG practices are 13% more likely to pay dividends. This suggests that ESG and dividends often act as complements rather than substitutes. More recent evidence by Salvi, Nirino, Battisti & Gianfrancesco (2024) across 3,207 European firms from (2018–2022) confirms that sustainability-oriented firms distribute higher dividends, with managers balancing ESG investments and shareholder returns. Supporting these findings, Benlemlih (2019) shows that high CSR (used as a proxy for ESG) U.S. firms pay more stable and higher dividends, as responsible practices mitigate agency problems associated with overinvestment. Collectively, these studies indicate that strong ESG or CSR performance is positively associated with both the stability and level of dividend payouts, suggesting that sustainability initiatives and shareholder value creation can coexist.

Our study complements and extends this literature by providing evidence from a consistent European institutional setting, focusing on ESG scores rather than CSR disclosures, examining each ESG pillar separately, and integrating governance characteristics to demonstrate how ESG and corporate governance jointly influence dividend decisions. Using Euronext-listed European firms, we highlight the differential impact of Environmental, Social, and Governance dimensions on dividend policy, while also considering ownership structure and board composition to capture the combined influence of ESG and governance on both the dividend payout ratio and dividend yield.

1.3 ESG in Shareholder and Stakeholder Views

The integration of Environmental, Social, and Governance (ESG) principles into corporate strategy has sparked ongoing debate between two foundational theories of corporate purpose: shareholder theory and stakeholder theory. This section explores how each theory interprets the role of ESG investments, highlighting the potential tensions and synergies between short-term financial returns and long-term sustainability objectives.

1.3.1 Shareholders Theory

Maximizing shareholder value is the central interest of shareholder theory (Friedman, 1970). Shareholder value refers to the wealth generated for shareholders through dividends and capital gains (Zhou & Bu, 2025). ESG investments and shareholder wealth raise important questions in the context of the trade-off between short-term and long-term perspectives. ESG indicates a company's ability to navigate long-term risks and capitalize on new opportunities; some investors may exhibit a bias toward underestimating long-term value creation, focusing instead on immediate returns. Investors with longer horizons tend to prefer firms with strong ESG performance, while short-term investors prioritize near-term profits, often at the expense of long-term sustainability (Matos, Barros

& Sarmento, 2020). From a shareholder perspective, Friedman (1970) argued that adopting SR policies can destroy shareholder wealth. Thus, managers should not allocate company resources to ESG activities if such actions reduce shareholder value. In the short term, ESG expenditures may be perceived as lowering dividend payouts, potentially discouraging investors and generating agency conflicts between managers (agents) and shareholders (principals). This is because the costs associated with ESG practices represent cash outflows that reduce current earnings, thereby diminishing shareholders' immediate profits (Salman, Djunaedi & Ardianto, 2024).

Krieger and Mauck (2024) support the shareholder theory by proposing a win–win scenario in which maximizing shareholder wealth and adopting high ESG standards are not mutually exclusive. Rather than creating a trade-off, ESG can complement shareholder value creation—especially when viewed through a long-term strategic lens. Firms that invest in ESG initiatives may achieve higher long-term profitability, aligning directly with the goals of maximizing shareholder wealth. This perspective suggests that ESG is not a diversion from shareholder interests but a potential pathway to enhance them.

1.3.2 Stakeholder theory

Freeman (1994) presents an alternative view, suggesting that effective management depends on how well a company maintains and manages good relationships with all stakeholders—including employees, customers, and suppliers—not just its shareholders. In this context, Salman, Djunaedi & Ardianto (2024) emphasize that stakeholder theory supports ESG investment not primarily to enhance shareholder wealth but to promote social welfare, strengthen community ties, and ensure good governance. Under this theory, managers may choose to reinvest profits or retain earnings for initiatives such as green technologies, social programs, or governance improvements, aiming to create long-term value for a broader set of stakeholders. While these actions may reduce short-term returns, they can still lead to enhanced long-term shareholder value through improved sustainability and risk management (Zhou & Bu, 2025). In support of this, studies have shown that firms with high ESG performance benefit from stronger stakeholder relationships and increased investor confidence (Krieger & Mauck, 2024; Benlemlih, 2019).

This perspective is further supported by existing theoretical frameworks. As stakeholder pressure increases, firms are more likely to adopt ESG initiatives as a means to address and reconcile potential conflicts between managers and various stakeholder groups. By engaging in ESG practices, companies can align managerial actions with the expectations and rights of both stakeholders and shareholders. A high ESG score across all three dimensions reflects a firm's comprehensive commitment to these broader responsibilities (Zahid, Taran, Khan & Chersan, 2023), reinforcing the view that ESG performance serves as a mechanism for conflict resolution and legitimacy-building in stakeholder-oriented firms. The dividend clientele effect suggests that investors choose firms whose dividend policies align with their preferences, such as income-oriented or growth-oriented investors (Allen, Bernardo & Welch, 2000). Low dividends might signal a departure from the expectations of certain clienteles, especially if ESG performance is prioritized over

immediate cash returns (Yang, Tang, Hu & Yao, 2025). Furthermore, the catering theory posits that firms adjust their dividend policies in response to investor demand, sometimes paying dividends to appease market pressures (Baker & Wurgler, 2004). For firms with strong ESG performance, the catering theory suggests that market sentiment toward ESG initiatives might influence dividend behavior. During periods when ESG investment is highly valued, firms may reduce payouts to reinvest in sustainability projects, resulting in abnormally low dividend yields.

1.4 Factors Affecting Dividend Decision

The decision to distribute dividends is influenced by a range of firm internal and external factors. These include sustainability, corporate governance mechanisms, and financial income, all of which shape a firm's ability and willingness to return earnings to shareholders. Understanding these factors is crucial for evaluating how firms strike a balance between retaining earnings for reinvestment and rewarding shareholders through dividend payouts.

1.4.1 ESG

Given that both dividends and ESG relate to firm spending decisions, the choice may often appear as an “either/or” dilemma: sometimes firms may forgo dividends to fund ESG initiatives, while other times they maintain dividend payments despite high ESG engagement. The financial capability channel has been employed to investigate this through earnings (e.g., earnings capability) or risk (e.g., income volatility). Three interrelated theories are emphasized: agency theory, signaling theory, and stakeholder theory (Zahid, Taran, Khan & Chersan, 2023), as well as management incentives (Sun, Li, Xie & Cheng, 2023).

Two main competing effects can be found in this relation. On one hand, some studies find that high ESG/CSR might actually correlate with higher or stable dividends. (Krieger & Mauck, 2024) found that, on average, firms are not forced to sacrifice dividends in favor of ESG spending. This is consistent with previous studies that have found a positive relationship between ESG and dividends (e.g. Zahid, Taran, Khan & Chersan, 2023; Bilyay-Erdogan, Ozturk Danisman & Demir, 2023; Benlemlih, 2019; Cheung, Hu & Schwiebert, 2018; Rakotomavo, 2012), and that high ESG engagement is also associated with more stable dividend policies (e.g., Matos, Barros & Sarmento, 2020).

To explain the impact of ESG score on dividend, we follow Bilyay-Erdogan, Ozturk, Danisman, & Demir (2023), who provide two key channels through which ESG performance can impact corporate dividends: the risk channel and the earnings channel. First, the risk channel. Firms with strong ESG performance can mitigate risks, contribute to resolving agency conflicts which theoretically leads to more efficient cash management and avoid anomalies in cash holdings (Yang, Tang, Hu & Yao, 2025), reduced operational risks, helps insulate firms from market uncertainty and reduces perceived financial risk by lowering both the cost of equity and debt (e.g., Apergis, Poufinas & Antonopoulos, 2022). Additionally, non-financial disclosures communicate effective risk management, reduce

information asymmetry, alleviate financial constraints, and help protect companies against lower stock volatility (Friske, Hoelscher & Nikolov, 2023; Zahid, Taran, Khan & Chersan, 2023). Better equipped to navigate regulatory transitions, reputational risks, and well-positioned for long-term growth, reinforcing perceptions of good governance and low idiosyncratic risk (Zhou & Bu, 2025; Chen, Li, Zeng & Zhu, 2023). This financial advantage allows firms to allocate more resources at a lower cost toward dividend distributions (Zahid, Taran, Khan & Chersan, 2023; Matos, Barros, & Sarmento, 2020).

The second mechanism linking ESG to dividends is the earnings channel, which emphasizes the role of ESG in enhancing profitability. Strong ESG practices are frequently associated with higher long-term earnings, driven by improved operational efficiency and risk management. This long-term orientation allows firms to capitalize on sustainable practices that yield steady financial returns over time (Krieger & Mauck, 2024). Furthermore, strategic ESG initiatives can create a competitive advantage (i.e., increase competitor costs to keep up with environmental efforts, etc.). thereby positioning the ESG-leading firm more favorably in the market (Krieger & Mauck, 2024). High ESG score activities serve as positive net present value (NPV) projects, increasing the firm's value and profitability (Aydoğmuş, Gülay, & Ergun, 2022). Similarly, ESG performance enhances firm valuation by building investor confidence and reducing capital costs. Furthermore, ESG-led initiatives—such as resource efficiency, waste reduction, and sustainable supply chain management—can generate substantial cost savings and enhance productivity and reputational capital (Kräussl, Oladiran & Stefanova, 2024). Consequently, improved ESG enables efficient cash allocation, thereby avoiding cash shortfalls that can lead to increased borrowing costs or missed investment opportunities (Yang, Liu & Su, 2025). Overall, firms with a strong presence in ESG activities are expected to achieve higher earnings streams with lower risk, enabling these companies to distribute more cash as dividends (Zahid, Taran, Khan & Chersan, 2023).

Moreover, agency cost plays a central role in shaping dividend policy based on the free cash flow theory (Jensen, 1986). When managers have access to excess cash flow alongside valuable investment opportunities, they may be inclined to overinvest. From this standpoint, dividend policy functions as a disciplinary mechanism to limit overinvestment in ESG initiatives, control agency problems related to free cash flow, and reinforce managerial discipline by reducing the amount of excess cash available. This approach prevents managers from using cash for self-serving purposes—such as reputational gains or career advancement—potentially mitigating conflicts between opportunistic managers and shareholders (Zahid, Taran, Khan & Chersan, 2023; Benlemlih, 2019; Matos, Barros & Sarmento, 2020). Furthermore, managers sustain dividends to manage conflicts with risk-averse shareholders who expect regular returns, while pursuing high ESG investment, thereby reducing agency conflict (Lucas, 2020). Further, Benlemlih (2019) argues that the effect of ESG on dividends reflects a combination of cash flows, risk, and growth opportunities.

Both dividends and ESG function as signals to the market. According to the signaling theory of dividends (Bhattacharya, 1979), corporate finance companies need to signal and convey information about their underlying quality to external stakeholders through observable and credible actions,

such as dividend payments, which convey information about a firm's prospects and expected future earnings. Thus, a high dividend level combined with high ESG scores sends a strong positive signal to financial markets and stakeholder groups (Benlemlih, 2019), indicating that a firm can meet stakeholders' expectations without inefficiently allocating resources to ESG activities (Chen, Li, Zeng & Zhu, 2023; Zhou & Bu, 2025). This boosts confidence in allocating funds to such firms, leading those with strong ESG profiles to pay higher dividends to reinforce their credibility (Zahid, Taran, Khan & Chersan, 2023). Overall, this perspective suggests a positive association between ESG engagement and dividend payouts. In this context, some studies propose that dividend policy may serve as a compensatory signal, with firms adjusting payouts to offset perceived risks or costs associated with ESG performance (Bilyay-Erdogan, Ozturk Danisman & Demir, 2023).

On the other hand, a negative effect can be found. The negative relationship between ESG performance and dividend payments is explained by some authors through relevant theoretical frameworks, the associated costs of ESG initiatives that directly compete with dividends for scarce internal resources (Rakotomavo, 2012), and the potential for opportunistic managerial behavior.

ESG investments typically involve high costs and often require substantial corporate resources. As a result, firms facing high ESG investment demands tend to prefer using internal funds, such as retained earnings. In situations where internal resources are scarce, companies may reduce or withhold dividend payments to conserve cash for these investments (Yang, Tang, Hu & Yao, 2025). Moreover, ESG engagement is associated with lower liquidity (Luo, 2022), which may further reduce the availability of cash for dividend distributions.

From the perspective of agency theory, Salman, Djunaedi & Ardianto (2024) argue that ESG investments can increase agency costs. Firms with high ESG engagement often hold excess liquidity, which provides managers with greater flexibility in capital expenditures. This flexibility can lead to opportunistic behavior—such as pursuing personal reputation-building—rather than maximizing shareholder value (Sun, Li, Xie & Cheng, 2023). Managers may retain earnings, redirect resources, or reinvest profits into ESG activities, thereby reducing dividend distributions and straining financial resources (Kräussl, Oladiran & Stefanova, 2024; Salman, Djunaedi & Ardianto, 2024; Zhou & Bu, 2025). Empirical evidence supports this view: firms with high ESG engagement often pay lower dividends (e.g., Lucas, 2020). These behaviors are commonly linked to governance failures, particularly in firms with weak oversight structures, where dividend payouts tend to be lower (Jensen & Meckling, 1976).

According to the catering theory, market sentiment toward ESG can influence dividend behavior. During periods when ESG initiatives are highly valued by investors, firms may reduce payouts to redirect funds toward sustainability projects, resulting in abnormally low dividends (Yang, Tang, Hu & Yao, 2025).

Signaling theory offers another perspective. Firms that disclose corporate social responsibility (CSR) information may use this disclosure as a signal of good management, long-term value, or financial stability. As such, these firms might reduce dividend payouts, relying on disclosure to partially substitute for traditional dividend signaling (Uyara, Wasiuzzaman, Kuzey & Karamand, 2024).

Finally, stakeholder theory suggests that ESG-oriented companies may prioritize long-term stakeholder value over immediate shareholder returns. (Donaldson & Preston, 1995) emphasize this shift in focus. Building on this, Yilmaz, Aksoy & Khan (2024) argue that firms with long-term ESG goals may intentionally reduce dividend payments to fund ESG initiatives, especially when reinvestment takes precedence (see also Benlemlih, 2019). While dividend payouts are typically viewed as indicators of sound governance and financial stability, abnormally low dividends may signal underlying issues, such as managerial opportunism or financial distress (Yang, Liu, & Su, 2025).

1.4.2 Corporate Governance

Corporate governance is a term that refers to the system of rules, practices, and processes by which a company is directed and controlled (Chartered Governance Institute UK & Ireland 2019). Corporate governance can affect ESG decisions, as it influences how managers allocate resources and communicate with stakeholders. La Porta, Lopez-de-Silanes, Shleifer and Vishny (2000) develop the idea that dividends and corporate governance mechanisms can be either substitutes for or complements to one another. If external corporate governance mechanisms allow the board and equity holders to impose a payout policy that helps limit managers' excessive spending to invest sub-optimally, then these two types of devices are complements. If, on the other hand, the board feels that there are enough other corporate governance elements in place to control management's behavior, then these two can be viewed as substitutes. Indeed, it builds on the idea that some institutional investors (who prefer dividends for tax reasons) represent the external governance mechanisms that interact with dividends. The presence of institutional investors increases the value of the firm because of the monitoring role they play, and because they help facilitate takeover activities (even if they are not directly involved in them). Thus, the board has an incentive to induce these shareholders to take a position in the firm, especially if the firm is likely to have excess cash. This setting suggests interesting dynamics between governance and payout (Farre-Mensa, Michaely & Schmalz, 2014).

Behavioral theories see market inefficiency (investor sentiment), investor biases, and managerial biases as the key drivers of dividend payments. There is some mixed empirical evidence about the link between managerial bias and dividend payout. Some studies find that CEOs who are optimistic about their firms' cash flows ("overconfident" is the term used) are less likely to pay out dividends, while others argue that managers will commit too quickly to paying dividends based on private signals. Deshmukh, Goel & Howe (2009) document that the level of payout (dividend yield) is lower for optimistic managers. The intuition behind the test is that managers with a buoyant belief in their firm's future prefer to invest cash in firm-high investments rather than pay it out to investors (Baker & Nofsinger, 2010). Conversely, managers who are more focused on meeting shareholder expectations or maintaining market confidence may limit ESG spending to preserve or increase dividends. It may be necessary for them to establish a reputation for not exploiting shareholders by

paying dividends. Managers object to the notion of using dividends as a ‘money burning machine’ to signal value (Farre-Mensa, Michaely & Schmalz, 2014).

Donaldson and Preston (1995) argue that managerial decisions are not made in a vacuum often reflect their motivations such as ego gratification and career advancement their own values, perceptions, and how they scan and assess their operating environment interpret, especially when incentives are reinforced through mechanisms such as excessive salaries and bonuses—frequently In this context, decisions to increase ESG score, may reflect managerial self-interest attempts to build reputational capital or align with personal values or external recognition, it becomes descriptively accurate to suggest that managers’ interests take precedence over those of other stakeholders. which may be diverted available funds from dividend payouts to support sustainability goals. Rather than maximize shareholder wealth, these variations underscore that dividend policy is not purely a financial decision, but one shaped by the individual judgment and ethical stance of the manager. From another stakeholder perspective, Mitchell, Agle, and Wood (1997) argue that the importance of stakeholders varies depending on how managers perceive their salience. When ESG-oriented stakeholders (like activist investors or regulators) are seen as more powerful and urgent than traditional shareholders, firms may prioritize ESG activities, even if it means reducing cash distributions to shareholders.

2. Research Methodology

This chapter describes the research design, data collection, sample characteristics, hypotheses, and the econometric models used to investigate the ESG–dividend relationship.

2.1 Objective of the study and Research Hypothesis

The primary objective of this study is to examine whether dividend distributions are affected by ESG scores within the European market. The study aims to understand how ESG may have differing effects on dividends, as an increase in ESG spending could reduce dividends due to higher costs or, alternatively, enhance dividends through improved firm performance. We introduce mediating variables to uncover the mechanisms through which ESG score impacts shareholder wealth.

The recent literature on this field suggests a positive relationship between CSR/ESG Performance and dividend payout (Benlemlih, 2019; Bilyay-Erdogan, Ozturk, Danisman, & Demir, 2023; Krieger & Mauck, 2024). There are two main perspectives. On the one hand, firms with high ESG performance are more likely to maintain or increase their dividends due to several factors. First, the risk channel explains that ESG reduces financial and operational risks, signaling greater stability, lowering capital costs, and enabling more predictable cash flows (Apergis, Poufinas, & Antonopoulos, 2022; Zahid, Taran, Khan, & Chersan, 2023; Friske, Hoelscher, & Nikolov, 2023). Second, the earnings channel highlights that ESG enhances long-term efficiency, competitive advantage, and cost savings, which improve profitability and support higher or more stable dividends (Krieger & Mauck, 2024; Aydoğmuş, Gülay & Ergun, 2020; Kräussl, Oladiran & Stefanova, 2024). Third, strong ESG performance reduces agency conflicts by signaling good governance and limiting managerial misuse of excess cash (Benlemlih, 2019; Matos, Barros & Sarmento, 2020). Finally, from a signaling theory perspective, the combination of ESG engagement and dividend payouts sends a stronger positive signal to investors about the firm's quality, thereby boosting confidence and firm value (Bhattacharya, 1979; Zhou & Bu, 2025). Overall, high ESG performance strengthens financial fundamentals and market confidence, thereby supporting or enhancing dividend payouts.

Conversely, on the other hand, high ESG engagement can lead to lower dividends due to competing internal demands and managerial discretion. ESG initiatives often require significant investments, which may compete with dividends for scarce internal funds, especially when liquidity is low (Rakotomavo, 2012; Luo, 2022; Yang, Liu & Su, 2025). Increased agency costs may arise when managers divert funds to ESG projects for personal reputational gains rather than maximizing shareholder value (Salman, Djunaedi & Ardianto, 2024; Sun, Li, Xie & Cheng, 2023). Firms may also use ESG disclosures as an alternative signal of quality, thereby reducing the need for high dividend payouts (Uyara, Wasiuzzaman, Kuzey & Karamand, 2024). From a stakeholder theory standpoint, ESG-oriented firms may prioritize long-term stakeholder interests over short-term shareholder returns, intentionally lowering dividend distributions (Donaldson & Preston, 1995). In sum, ESG

investments require substantial resources and can increase managerial discretion, potentially leading to reduced dividend payments (Yilmaz, Aksoy & Khan, 2024).

Although these opposing views, it is expected that the first will be more relevant. To support this objective, the following research hypotheses are proposed:

Null Hypothesis (H0): ESG scores are positively associated with dividend payout ratios among dividend-paying firms.

2.2 Description of Data Collection

Data for this study were collected from multiple reliable sources to ensure comprehensive coverage and accuracy. The initial list of companies was drawn from the official Euronext equities list, covering firms across 20 European territories. This resulted in a total of 1790 firm-year observations spanning the period from 2019 to 2023, initially including 358 listed firms.

Dividend and financial data were sourced from Investing, a publicly available platform known for transparent data collection and verification processes. These data provide detailed information on firms' dividend payouts, profitability, and other relevant financial metrics. ESG scores for the period 2019 to 2023 were obtained from the London Stock Exchange Group (LSEG), formerly known as Refinitiv. LSEG's ESG ratings provide an objective, data-driven assessment of a company's ESG performance, commitment, and effectiveness. The scores are based on over 870 metrics, including 186 core indicators derived from publicly disclosed information. These metrics are selected for comparability, impact, data availability, and industry relevance, allowing for tailored evaluation across different sectors. The ESG metrics are organized into 10 categories, which collectively form the three pillars of ESG: Environmental, Social, and Governance (see Figure 3). The final ESG score is calculated by summing the scores within each pillar, producing a score ranging from 0 to 100. The environmental score ranges from 0 to 100%. The Environmental, Social and Governance score Ranges from 0 to 100%. Consists of 56 indicators: nine for CSR strategy, 12 for shareholders, and 35 for management. These scores are commonly classified into quartiles for interpretability. A score above 70 indicates strong ESG performance. A reading below 50 may be viewed as a warning sign, especially for investors who prioritize sustainability[1]. 0–25: Poor; 26–50: Satisfactory; 51–75: Good; 76–100: Excellent. This classification enables a clearer interpretation of a company's ESG standing and facilitates benchmarking against peers.

To enrich the analysis and address potential moderating factors affecting dividend policy, additional data on corporate governance were collected. Specifically, information regarding board composition — including the presence of independent directors — and ownership structure was gathered from each company's official website at the end of their respective fiscal years. This approach ensures that governance data is up-to-date and reliable, reflecting the international nature of the firms.

[1] https://www.lseg.com/content/dam/data-analytics/en_us/documents/methodology/lseg-esg-scores-methodology.pdf

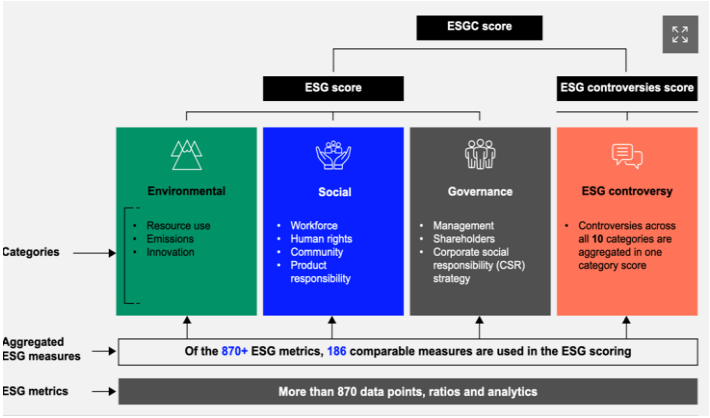

Figure 1. A closer look at the category of ESG scores

Source: ESG Scores from LSEG methodology (2024, p.4).

The control variables related to corporate governance and ownership structure: To account for the influence of corporate governance on dividend policy. We retrieve information on ownership by types of investors as a percentage of shares held at the end of the 2023 fiscal year (e.g., government, public institutions, individuals, financial institutions) as reported by Fiorillo and Santilli (2024).

2.3. Description of Data Analysis

To examine the impact of ESG performance on firms' dividend policy, we employed an empirical model grounded in prior literature. The empirical model is estimated using panel data methods (OLS/fixed effects). The dependent variable is the dividend payout ratio. The main independent variables are the overall ESG score and its environmental (E), social (S), and governance (G) sub-scores. The control variables include firm size, profitability (ROA), leverage (LEV), cash holdings, growth, and Tobin's Q (Lucas, 2020; Saeed & Zamir, 2021; Salvi, Nirino, Battisti & Gianfrancesco, 2024). The baseline regression model is specified as follows:

$$DIVPR_{i,t} = \beta_0 + \beta_1 ESG\mathit{SCORE}_{i,t} + \beta_2 SIZE_{i,t} + \beta_3 ROA_{i,t} + \beta_4 LEV_{i,t} + \beta_5 CASH_{i,t} + \beta_6 MBR_{i,t} + \beta_7 Tobin\ Q_{i,t} + \varepsilon_{i,t} \quad (1)$$

The dependent variable is $DIV_{i,t}$, defined as the ratio of total dividends distributed to shareholders to the total assets (Benlemlih, 2019). The main independent variables are the yearly ESG score and, alternatively, each of its three sub-components: the environmental (Env), social (Soc), and governance (Gov) scores, obtained from the Refinitiv database. $SCORE_{i,t}$ represents the aggregate ESG score of a given firm in a given year, each score ranges from 0 to 100. The Environmental, Social, and Governance Score ranges from 0 to 100%.

The control variables are consistent with existing studies, we adopt an empirical approach grounded in prior literature and include a set of control variables commonly associated with dividend decisions. $SIZEi,\ t$, measured as the natural logarithm of total assets (Zahid, Taran, Khan & Chersan, 2023); ROA $i,\ t$ a measure of profitability defined as the ratio between operating income and total assets (Salvi, Nirino, Battisti & Gianfrancesco, 2024); $CASHi,t$, calculated as cash and cash-equivalents divided by total assets; LEV, calculated as total firm liabilities over firm total; Growth proxied by the

market-to-book (MBR) ratio. MBR is the ratio of the market value of equity to the book value of equity (Saeed, Zamir, 2021). “Tobin's Q” also emerges as a fundamental metric associated with contributions that involve both firm performance and sustainability in terms of ESG. All variables are measured on an annual basis for each firm in the sample.

All variables are important for a reason in this study, as follows:

- **Size**: Firm size, typically measured by the natural logarithm of total assets, can be negatively associated with dividend payouts. These firms may prefer to retain earnings to fund growth opportunities, acquisitions, or other investments rather than pay out dividends. Additionally, larger firms might face more complex organizational structures and agency conflicts, which could lead to more conservative dividend policies to maintain internal control and financial flexibility (Zahid, Taran, Khan & Chersan, 2023).
- **Leverage:** is negatively associated with dividend payouts, as highly leveraged firms face greater pressure to meet debt obligations, and creditors may impose restrictions on dividend distributions to protect their interests (Cheung, Hu & Schwiebert, 2018). However, ESG scores are correlated with lower debt financing costs (Zahid, Taran, Khan & Chersan, 2023)
- **ROA:** key determinants of business profitability. Consumers appreciate corporate social and environmental commitments, which boost revenues by establishing brand equity, improving stakeholder interactions, increasing staff productivity, and enhancing asset allocation. It can lead to a change in the sales market share, resulting in favorable financial outcomes and enhancing the corporate ability to pay dividends (Cheung, Hu & Schwiebert, 2018).
- **Cash holdings**: represented by cash and short-term investments scaled by total assets. From an agency conflicts perspective, managers may increase the cash holdings, reducing dividend payments. Thus, a negative relationship is expected. From another view, managers might mitigate the agency costs of free cash flows by using dividends. Consequently, it should be expected to be a positive relationship. In conclusion, we can expect either a positive or a negative relationship (Benlemlih, 2019).
- **Growth:** According to the firm life-cycle hypothesis, companies with more promising growth prospects should retain their profit for reinvestment, contributing to business growth. In contrast, companies with less promising prospects of growth should be able to benefit from their cash flow by increasing dividend payments (Zahid, Taran, Khan & Chersan, 2023)

Then, we introduce additional variables to strengthen our analysis through a robustness analysis. The following model is used as a baseline for robustness analysis:

$$\text{DIVPR}_{i,t} = \beta_0 + \beta_1 \text{ESG}\mathcal{SCORE}_{i,t} + \beta_2 SIZE_{i,t} + \beta_3 ROA_{i,t} + \beta_4 LEV_{i,t} + \beta_5 CASH_{i,t} + \beta_6 MBRi,t + \beta_7 Tobin\ Q_{i,t} + \beta_8 BINDP_{i,t} + \beta_9 EXTOWN_{i,t} + \beta_{10} INOWN_{i,t} + \beta_{11} FINST_{i,t} + \varepsilon_{i,t} \quad (2)$$

Where the variables are the following:

- BSize is measured as the total number of directors on a company’s board;
- BInd is defined as the ratio of independent directors to the total number of directors on the board (Endrikat, De Villiers, Guenther & Guenther, 2021).

- EXTOWN, are the external owners, and are measured as the percentage of shares held by various investor groups at the end of the 2023 fiscal year (e.g., government, public institutions, individuals, and financial firms) (Fiorillo & Santilli, 2024).
- FINST: institutional ownership as a percentage of shares held by financial institutions in a specific firm, including pension funds, insurance companies, and banks (Saeed & Zamir, 2021; Fiorillo & Santilli, 2024).

Board size and Board independence as mediating variables are known to affect corporate decisions by enhancing shareholder protection and reducing agency conflicts and managerial opportunism (Zahid, Taran, Khan & Chersan, 2023). A larger board may imply a dilution of power, but it may also potentially lead to more effective monitoring and objective oversight. Higher board independence is often associated with improved corporate governance and better alignment with shareholder interests (Endrikat, De Villiers, Guenther & Guenther, 2021).

Additionally, ESG performance has varying impacts on dividend payouts, depending on the ownership structure. For companies with dispersed ownership, where shareholders have weaker supervisory power and management has more control over decision-making, the effect of ESG performance in reducing abnormal payouts is stronger compared to companies with concentrated ownership (Yang, Tang, Hu & Yao, 2025). The variables are defined in the table below.

Table 2. Definition of Variables Used in the Regression Models

Variable	**Description**
DIVPR	Dividend Payout Ratio: The ratio of total dividends to total assets for the firm.
ESG Score	ESG Score: Environmental, Social, and Governance (ESG) performance score.
SIZE	Firm Size: Natural logarithm of total assets.
ROA	Return on Assets: Net income divided by total assets.
LEV	Financial Leverage: Ratio of total debt to total assets.
CASH	Cash Holdings: Cash and cash equivalents as a percentage of total assets.
MBR	Market-to-Book Ratio: Market value of equity divided by book value of equity.
TobinQ	Tobin's Q: Book value of total assets, minus the book value of equity, plus the market value of equity, all divided by the book value of total assets
BSIZE	Board Size: Total number of directors on the board.
BINDP	Board Independence: Proportion of independent directors on the board.
EXTOWN	External Ownership: Percentage of shares held by external (non-insider) shareholders.
INOWN	Internal Ownership: Percentage of shares held by company insiders or executives.
FINST	Institutional Ownership: Percentage of shares held by institutional investors (e.g., banks, funds).

Source: author`s own elaboration

2.4 Data Sample

The population for this study consists of all publicly listed firms on the Euronext stock exchange across Europe. This includes firms from countries such as France, Germany, Italy, the Netherlands, Norway, Belgium, the United States (listed on Euronext Europe), Spain, Portugal, Ireland, Austria, Finland, and Luxembourg. Europe was selected as the geographical focus due to its strong emphasis on ESG reporting and sustainable development. European firms are recognized leaders in corporate sustainability; for example, countries like Sweden, Spain, France, the UK, and the Netherlands have sustainability reporting rates exceeding 90%. Furthermore, France, Sweden, the Netherlands, and Norway are among the leaders in integrated reporting, while Finland, France, and the UK excel in incorporating sustainability information into their annual reports. The UE has also implemented several directives that advance ESG regulations and reporting standards, such as the recent directive on the disclosure of non-financial information in management reports. The PRI and updated UE fund labeling schemes underscore the institutionalization of ESG by imposing stricter disclosure and asset requirements. This regulatory and cultural environment makes Europe an ideal population for studying ESG performance.

We utilize firm-level data from 358 European countries and 13 US firms listed on the Euronext stock exchange, for the years 2019-2023. To ensure comparability and data quality, we form our sample by excluding financial firms (e.g., Banks, assurance firms) due to their distinct disclosure requirements and investment policies (Benlemlih, 2019). Additionally, firms without available ESG scores were removed, as ESG performance is a key variable in this study. Observations with missing or erroneous data were also excluded, along with firms that did not pay dividends during the study period, as the focus is on dividend payout policies. After applying these exclusion criteria and removing duplicate records, the final sample comprises 358 firms from various European countries. The final sample is representative of the population in terms of geographic coverage and provides sufficient data to analyze the relationship between ESG performance and dividend payout behavior. The final sample comprises 1,785 firm-year observations. Table 3 presents the distribution of firms across the 21 countries.

Table 3. Sample Composition across Countries

Countries	Number of companies	N. of observations	Firm distribution (%)	Countries	Number of companies	N. of observations	Firm distribution (%)
France	102	510	28,49	US	13	65	3,63
Germany	62	310	17,32	Spain	7	35	1,96
Italy	52	260	14,53	Portugal	8	40	2,23
Amsterdam	37	185	10,34	Ireland	6	30	1,68
Norway	32	160	8,94	Austria	3	15	0,84
Belgium	26	130	7,26	Finland	5	25	1,4
				Luxembourg	5	25	1,4

Source: Authors' own calculations.

3. Empirical Results Analysis

This section presents the empirical results of the study, including descriptive statistics, correlations, and regression analyses that investigate the effects of ESG Scores and firm-specific characteristics on dividend payments for the period 2019-2023.

3.1 Sample Characterization

Figure 2 presents the average dividend payments during the study period. Table 3 presents the sample profile across countries. The largest portion of firms comes from France (28.5%), followed by Germany (17.3%) and Italy (14.8%). Finland records the highest average Dividend Payment Ratio (DPR) at 4.34, followed by Spain (3.63) and Norway (3.42), while Luxembourg has the lowest. Overall, the sample provides a balanced representation of firms across European countries and the United States. The data also reveal a clear contrast between Northern and Western European countries, with Northern nations generally reporting higher dividend payout levels.

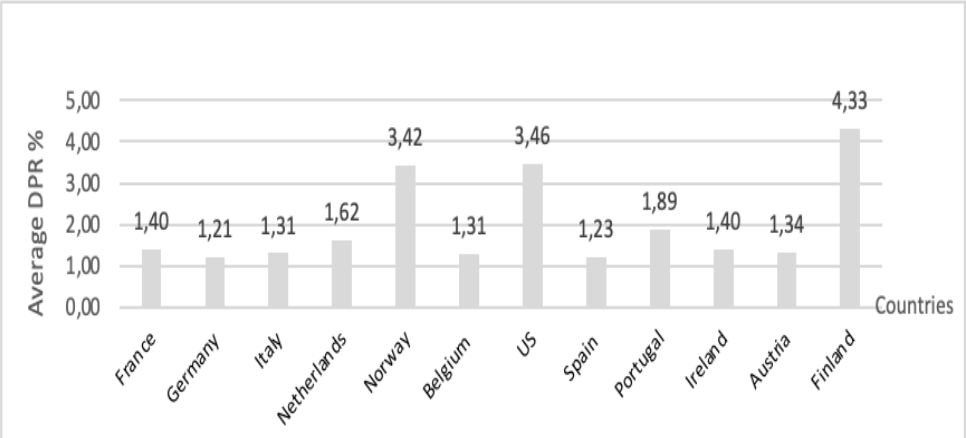

Figure 2. Dividend Payment Ratio (DPR) across countries

Source: author`s own elaboration

Figure 3 presents the evolution of the average dividend payout ratio for the sample firms. On average, companies distributed dividends equivalent to 2.61% of total assets in 2019, increasing to 2.82% by 2023. In terms of ESG performance, the average total ESG score rose marginally from 66 in 2019 to 67 in 2023. Although the increase in dividend payouts is modest, it may reflect improvements in profitability associated with ESG engagement. Overall, these results indicate that ESG initiatives do not appear to impose substantial costs on shareholders.

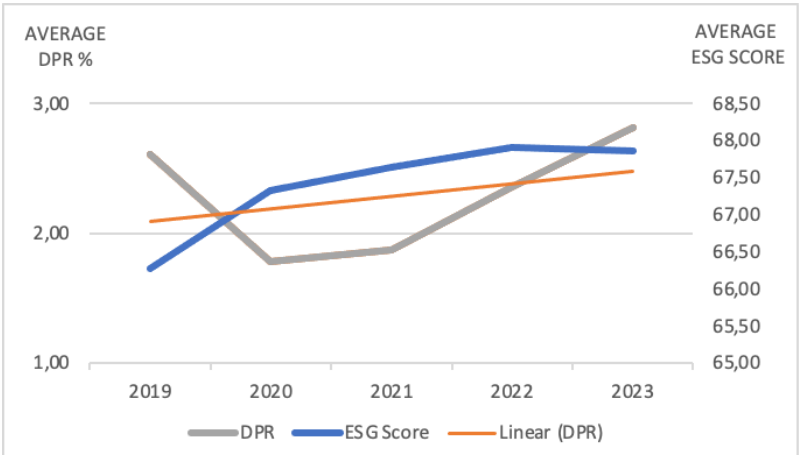

Figure 3. Dividend Payment Ratio (DPR) and ESG Score from 2019 to 2023.

Source: Author's own elaboration

3.2 Descriptive Statistics of Variables

Table 4 summarizes the descriptive statistics of ESG Score, which is our primary focus, along with the control variables included in the study.

Table 4. Descriptive Statistics of the Main Variable — DPR

Variable	Obs.	Média	Median	Standard Deviation	Min	Max
DPR	1772	2.28	1.40	4.72	0.00	87.7
Div Yield	1772	3.20	2.08	5.02	0.00	75.0

Source**:** Author's own elaboration. The definition of variables is in Table 2.

The mean of our dependent variable, dividends, is 2.28, as shown in Table 2. This indicates that, on average, firms paid dividends equivalent to 2.28% of total assets from 2019 to 2023, representing a slight decrease from the 2.78% reported for the period 2015 to 2019 (Lucas, 2020). However, there is notable variation in dividend payouts across firms during our study period, reflected by a standard deviation of approximately 4.72. The maximum dividend ratio observed is 87.7%, while the minimum is zero.

The ESG score has an average score of 67.4 with a median of 71.0, suggesting a moderately high level of ESG performance across the sample. The relatively low standard deviation (16.7) indicates moderate variability among firms' ESG scores, which range from 3.0 to 95.0, highlighting the presence of both underperformers and leaders in ESG practices. Breaking down the ESG components, the Environmental (E) component averages 65.5, with a larger dispersion (SD = 21.6) and values ranging from 0 to 99, showing wide variation in environmental performance. The Social (S) score is the highest on average at 72.8, with a median of 77.0 and a standard deviation of 18.6, suggesting generally stronger social practices across firms. The Governance (G) component has the lowest mean at 61.2 and a standard deviation of 21.2, reflecting notable heterogeneity in governance, with scores ranging from 4 to 99.

Table 5. Descriptive Statistics of Independent Variables

Variable	Average	Median	Standard Deviation	Minimum	Maximum
ESGScore	67.4	71.0	16.7	3.00	95.0
E	65.5	71.0	21.6	0.00	99.0
S	72.8	77.0	18.6	1.00	98.0
G	61.2	64.0	21.2	4.00	99.0
Size	9.06	9.11	1.73	2.78	14.3
ROA	6.05	5.59	7.28	-66.9	46.9
LEV	61.2	61.3	18.4	0.00	250.
CASH	11.13	8.65	11.4	0.00	92.
MBR	3.37	1.90	7.42	-68.0	131.
Tobin Q	1.63	1.08	6.39	-64.8	100.
EXTOWN	87.9	96.9	19.2	0.00	100.
INOWN	7.05	0.500	15.5	0.00	80.5
FINST	4.65	0.00	10.9	0.00	92.
BSize	11	10.0	3.28	3.00	20.0
BINDP	41,9	46.2	30.6	0.00	100.

Notes: The 5% (two-tailed) critical value is 0.0464 for n = 1784. The definition of variables is in Table 2.

Source: Author's own elaboration

Financial leverage (LEV) and cash holding ratios have higher standard deviations than corporate size, ROA Growth, and Tobin's Q, indicating various characteristics of the firms in terms of debt, the value of assets, profitability, and even financial loss, market valuation, maturity, and investment opportunities. Regarding profitability, for each 100 EUR invested in assets, firms generate approximately 6.05 EUR on average. In terms of liquidity, cash holdings range from 0.00% to 92.0% of total assets, with an average of 11.2%, reflecting the varying cash management strategies employed by firms. In terms of leverage, firms present, on average, 61.2% of debt relative to total assets, with some highly leveraged firms reaching up to 250%, showing considerable variation in capital structure policies. Board independence is 41.9 percent on average. Board size seems to vary from 3 to 20 members, with an average of eleven directors. The average for independent board members is around 41.9 percent of the companies.

Table 6 presents the Pearson pairwise correlation coefficients among the key independent and dependent variables examined in this study. We find that some of our variables are associated with dividend payout measures, as predicted by prior studies. This shows the relevance of the variables used in our research. Overall, we do not find any high correlation among our control variables, which confirms the absence of any multicollinearity issues in our regression analyses.

Table 6. Correlation analysis

	DP	DividYield	ESGScore	Size	ROA	Lev	CASH	MBR	Tobin Q
DP	1								
DividYield	0.2930	1							
ESGScore	0.0366	0.0777	1						
Size	-0.0779	0.1687	0.6020	1					
PROF	0.2420	0.0818	0.0793	0.0715	1				
Lev	-0.0950	0.0070	0.0524	0.0738	-0.3402	1			
CASH	0.0368	-0.1192	-0.1088	-0.1851	-0.0311	0.0308	1		
MBR	0.1295	-0.0074	-0.0583	-0.0470	0.1948	-0.0635	0.2376	1	
Tobin Q	-0.0337	-0.0594	-0.0709	-0.1153	-0.0499	-0.0380	0.0995	0.2196	1

Notes: The 5% (two-tailed) critical value is 0.0464 for n = 1784. The definition of variables is in Table 2.
Source: Author's own elaboration.

3.3. Multivariate Regression Results

This subsection presents the outcomes of empirical models testing the relationships between the main variables, such as Dividend Payout Ratio (DivPR) and firm ESG score, along with control variables. Alternative specifications, such as the Dividend Yield (DivYield), may be included to assess the robustness of the findings. Tables and figures should clearly show coefficients, standard errors, significance levels, and other relevant statistics.

3.3.1 Baseline Results

Table 7 presents the baseline results of our models, which were obtained through a panel ordinary least squares (OLS) regression with year-fixed effects. The initial dataset had 1785 observations, but the OLS regressions reduced this to 1533 due to listwise deletion, excluding firms with any missing values in the model's variables.

Each column of the table presents the results of the OLS regression estimation, and from now on, we will refer to each column as the Panel or the estimated Model, which will have the same meaning. In Panel 1, the coefficient of the ESG score variable is positive and significant at the 1% level. A one-point increase in the ESG score is estimated to raise the ratio of cash dividends to total assets by approximately 0.015 percentage points. This result suggests that higher ESG scores play a meaningful role in dividend payouts, a finding supported by previous research (Ryu, Ryu & Yang, 2025; Bilyay-Erdogan, Ozturk Danisman & Demir, 2023). This implies that ESG investments are positive net present value (NPV) projects—expected to generate more cash flow than they cost (Yang, Liu & Su, 2025)—and therefore create shareholder value. Next, the main model is replicated by replacing the combined ESG score with the individual environmental, social, and governance pillar scores as independent variables. Panels 2, 3, and 4 capture the effects of these individual components. All three dimensions—environmental, social, and governance—positively and significantly influence dividend payouts. The environmental and social scores (Panels 2 and 3) show positive and significant effects at the 1% level, while the governance score (Panel 4) demonstrates the strongest significance ($p < 0.01$). These results align with the findings of Bilyay-Erdogan, Ozturk

Danisman, and Demir (2023), who argue that each ESG pillar plays a crucial role in shaping dividend policy and contributes to higher corporate dividend distributions.

Table 7. Baseline regression results.

	DivPR			
	1	**2**	**3**	**4**
Const	0,819 **	0,859 **	0,821 **	0,735 *
	0,500	0,391	0,401	0,287
ESGScore	0,015 ***			
	0,006			
E		0.0073 **		
		0.0028		
S			0.0115 **	
			0.0041	
G				0.0121 ***
				0.0030
Size	(0.06)	(0.0180)	(0.0944) **	(0.027)
	0.0364	0.0385	0.0437	0.0402
ROA	0.114 ***	0.1242 ***	0.1312 ***	0.1334 ***
	0.0100	0.0102	0.0124	0.0119
LEV	(0.005) *	(0.004)	(0.005) *	(0.003)
	0.003	0.0027	0.0029	0.0026
CASH	(0.006)	(0.002)	(0.006)	(0.003)
	0.008	0.0075	0.0075	0.0071
MBR	0.018 *	0.0340 **	0.0303 ***	0.0433 ***
	0.007	0.0123	0.0110	0.0128
TobinQ	0.141 ***	0.1227 ***	0.1344	0.1360
	0.0281	0.0281	0.0275	0.0249
N	1533	1533	1533	1533
R^2	0,1328	0,1308	0,1293	0,1378
Adj. R^2	0,1289	0,1268	0,1253	0,1339

Note: This table presents the OLS regression results, which have been corrected for heteroskedasticity. The dependent variable is the dividend payout ratio. All independent variables are explained in Table 2. The first line in each variable is the coefficient, and the line below is the standard errors of the estimated variable. *** i.e. significant < 0.01; **i.e. significant <0.05;* i.e. significant <0.1

Source: Author's own elaboration

Regarding the control variables, the negative coefficient on firm size suggests that managers of larger firms may misuse excess free cash flow for personal benefit or inefficient projects, supporting the agency cost theory (Jensen, 1986). The coefficient of leverage (LEV) is negative and significant at the 1% level, indicating that highly leveraged firms tend to pay lower dividends due to the burden of higher interest payments. This finding supports the notion that debt serves as a substitute for dividend payments, consistent with the results of previous studies (Ryu, Ryu & Yang, 2025; Matos, Barros & Sarmento, 2020; Benlemlih, 2019). Cash holdings are also statistically significant at the 5% level. This result may reflect agency conflicts, whereby managers prefer to retain excess cash or invest in short-term assets rather than distribute dividends to shareholders (Benlemlih, 2019). In contrast, profitability, growth, and Tobin's Q exhibit statistically significant positive effects on dividend payments at the 1% significance level (Salvi, Nirino, Battisti & Gianfrancesco, 2024). This reinforces the notion that profitability is a key determinant of a firm's capacity to pay dividends, suggesting that

highly profitable firms generate greater free cash flows and, consequently, distribute higher dividends. This behavior may also serve as a mechanism to mitigate the overinvestment problem by reducing excess cash available to managers.

The results validate the hypothesis that ESG score is positively and significantly related to dividend payout ratios, challenging the notion that high ESG spending requires sacrificing dividends. This finding aligns with prior research (Benlemlih, 2019; Krieger & Mauck, 2024; Bilyay-Erdogan, Ozturk Danisman & Demir, 2023; Salvi, Nirino, Battisti & Gianfrancesco, 2024).

Table 8 presents the results using an alternative measure of dividend payout, dividend yield, to assess the impact of ESG performance on market-based dividend returns

Table 8. Regression Results

	DIV YIELD				
	5	**6**	**7**	**8**	**9**
Const	(0.704) 0.787				
ESG Score	(0.008) 0.009				0,019 *** 0,007
E		0.016 0.005			
S			(0.015) * 0.0081		
G				0.015 0.006	
Size	0.439*** 0.089	0.417 *** 0,085	0.4789 *** 0.0820	0.377 *** 0,073	
ROA	0.062*** 0.018	0.052 *** 0.015	0.0624 *** 0.0173	0.057 *** 0.0163	0.0497 *** 0.0134
LEV	0.008 0.007	0.015 ** 0.006	0.010 0.007	0.0146 0.0065	0.0136 *** 0.0051
CASH	(0.041) *** 0.009	(0.042) *** 0.0088	(0.042) *** 0.010	(0.041) *** 0.0069	(0.039) *** 0.0075
MBR	(0.016) 0.017	(0.002) 0.0145	(0.018) 0.017	(0.01) 0.015	7.9e-05 0.0081
TobinQ	(0.028) 0.021	0.0079 0.0195	0.015 0.021	0.018 0.020	0.0082 0.0153
N	1533	1533	1533	1532	1533
R^2	0.04584	0,0383	0,033	0,044	0,0538
Adj. R^2	0,00501	0,0345	0,0293	0,04	0,00501

Note: This table presents the OLS regression results, which have been corrected for heteroskedasticity. The dependent variable is Dividend Yield. All independent variables are explained in Table 2. The first line in each variable is the coefficient, and the line below is the standard errors of the estimated variable. *** i.e. significant < 0.01; **i.e. significant <0.05; * i.e. significant <0.1

Source: Author's own elaboration

Columns 5–9 replicate the analysis with dividend yield as the dependent variable. In contrast to the findings in Table 7, Column 5 indicates that the overall ESG score has no significant negative impact on the dividend yield. ESG performance does not exhibit a direct significant impact on dividend yield when firm size is included as a control variable. However, when firm size is excluded from the model,

the ESG score becomes positive and statistically significant at the 1% level (coefficient = 0.18), indicating that ESG can independently influence dividend yield in the absence of firm size.

We provide deeper insights into the effects of the individual ESG pillars on dividend yield. Models (6) and (8) show a positive but statistically insignificant association at the 5% level. In contrast, the social (SOC) variable in Model (7) exhibits a negative relationship, with a coefficient of –0.015, which is statistically significant at the 5% level. The lack of significance for the environmental (ENV) and governance (GOV) pillars may suggest that these dimensions are either less directly relevant to dividend yield or their effects are already captured by other financial and operational variables.

3.3.2 Robustness Analysis

This sub-section presents extended regression models that explore the relationship between ESG scores and dividend payouts, incorporating factors such as ownership structure and governance mechanisms. In all models, the dependent variable is the Dividend Payout Ratio (DivPR). Various model specifications introduce different ownership and board-related variables (see Table 9).

Table 9. The moderating role of governance ESG-dividend policy.

	DIVPR				
	1	**2**	**3**	**4**	**5**
ESG Score	0.0185 ***	0.016 ***	0.0208 ***	0,0162 ***	0.016 ***
	0.0068	0.004	0.0062	0.0042	0.002
Size	0.0641	(0.009)	(0.0811)	(0.024)	0,002
	0.0647	0.027	0.0743	0.032	0.029
ROA	0.1885 ***	0.138 ***	0.1711***	0.123 ***	0.121 ***
	0.0294	0.011	0.026	0.011	0.011
LEV	(0.003)	(0,003)	0.001	(0.004)	(0,003)
	0.0048	0.003	0.006	0.003	0,003
CASH	(0.003)	0.007	0.0047	0.008	0.010
	0.0151	0.008	0.018	0.007	0.008
MBR	(0.033)	0.056 ***	(0.01)	0.056 ***	0.057
	0.025	0.009	0.013	0.013	0.012
EXTOWN	(0.015) **				
	0.005				
INOWN		0.006 *			
		0.003			
FINST			0.018 *		
			0.011		
BSIZE				0,029 *	
				0,015	
BINDP					0.001
					0,002
N	1533	1533	1533	1533	1533
R^2	0.2344	0.1686	0.1704	0.1112	0.1053
ADJ R^2	0.1931	0.3910	0.1516	0.0517	0.0423

Note: This table presents the OLS regression results, which have been corrected for heteroskedasticity. The dependent variable is dividend payout ratio. All independent variables are explained in Table 2. The first line in each variable is the coefficient, and the line below is the standard errors of the estimated variable. *** i.e. significant < 0.01; **i.e. significant <0.05; * i.e. significant <0.1

Source: Author's own elaboration

Table 9 shows that the ESG score has a positive and significant effect on dividend policy across all model specifications. This finding is consistent with the main results and confirms that firms with higher ESG scores tend to distribute larger dividends. Profitability (ROA) remains a key determinant, consistently positive and significant, whereas firm size, leverage, and cash holdings exhibit negative or statistically insignificant effects. Firm growth generally reduces dividend payouts, particularly in some specifications, suggesting that firms with higher growth rates have more investment opportunities, thereby reducing dividend distributions in favor of increased investment (Ryu, Ryu & Yang, 2025). Regarding ownership factors, ownership variables are introduced in Models 1–3. External ownership (EXTOWN) shows a negative and significant coefficient ($p < 0.05$), indicating that firms with more dispersed external ownership tend to pay lower dividends. Insider ownership (INSOWN) has a positive and weakly significant effect ($\beta = 0.006$, $p < 0.01$), suggesting that higher insider ownership aligns managerial and shareholder interests, potentially leading to more generous dividend policies. These results are consistent with previous findings (Yilmaz, Aksoy & Khan, 2024). Financial institutional ownership (FINSTH) shows a positive but marginally significant ($p = 0.0818$), implying that firms with institutional investor presence may be slightly more inclined to distribute dividends. This may reflect institutional pressure for regular returns or the tendency of managers of undervalued firms to increase dividends to attract institutional investors (Farre-Mensa, Michaely & Schmalz, 2014). In terms of board structure, board characteristics are included in Models 4 and 5. Board size (Bsize) has a positive and significant effect ($p < 0.10$), indicating that larger boards may enhance monitoring and promote responsible payout policies. Board independence (Bindp), although positive, is statistically insignificant, suggesting that independence alone does not substantially influence dividend decisions in this sample.

The results highlight the mediating role of ownership structure and board characteristics in the relationship between ESG score and dividend payouts. Specifically, insider ownership is positively associated with dividend payouts, whereas firms with higher proportions of foreign institutional investors exhibit lower payout ratios. This can be explained through agency theory (Jensen, 1986): higher insider ownership may lead to entrenchment, where insiders prioritize their personal interests over those of other shareholders. Dividends then serve as a monitoring mechanism to counteract these entrenchment-related agency problems. Managers may also prefer to maintain control and secure their positions, avoiding the agency costs of external equity through regular dividend payments (Jensen, 1986; Jensen & Meckling, 1976; Benlemlih, 2019). Importantly, these ownership structures mediate the effect of ESG on dividend payouts. Strong ESG practices often improve operational efficiency, risk management, and profitability, but the translation of these improvements into dividend distribution depends on the alignment of managerial incentives with shareholder interests. Insider ownership amplifies the positive effect of ESG on dividends by ensuring that managers balance sustainability investments with shareholder returns, whereas foreign institutional ownership may dampen it due to lower pressure for immediate payouts.

Larger boards are better able to monitor management and guide strategic decisions that balance ESG initiatives and dividend payouts (Endrikat, De Villiers, Guenther & Guenther, 2021). In contrast, board independence appears insignificant in influencing dividends. Yuan, Shang, Yu & Yu (2024) explain that independent directors serving on multiple boards may have diluted monitoring capacity, reducing their influence on dividend policy. Thus, while board size strengthens the ESG–dividend link, board independence alone does not. Overall, our findings suggest that ownership structure and board size act as key channels through which ESG performance translates into higher dividend payouts, highlighting the importance of governance mechanisms in aligning sustainability initiatives with shareholder value.

3.4 Discussion

From a financial economics perspective, these findings can be interpreted through several theoretical lenses. First, according to agency cost theory (Jensen, 1986), the positive and significant relationship between ESG scores and dividend payouts suggests that firms with stronger sustainability practices use dividends as a mechanism to limit managerial discretion over free cash flows and mitigate potential overinvestment in non-value-maximizing projects (Benlemlih, 2019). In particular, the results for the governance pillar support the argument that strong ESG governance mechanisms reduce agency costs by improving transparency and aligning managerial actions with shareholder interests (Benlemlih, 2019; Matos, Barros & Sarmento, 2020). Second, according to dividend signaling theory (Bhattacharya, 1979), a high ESG score combined with consistent dividend payouts projects an image of responsible corporate behavior and financial health (Benlemlih, 2019; Zhou & Bu, 2025). Third, our findings also align with stakeholder theory, which posits that firms balance the interests of multiple stakeholders by engaging in responsible corporate behavior while simultaneously returning value to shareholders. By doing so, these firms may lower their cost of capital, enhance their reputation in capital markets (Benlemlih, 2019), and secure a more stable investor base (Ryu, Ryu & Yang, 2025; Kräussl, Oladiran & Stefanova, 2024).

Our research highlights the role of the board of directors and ownership structure in the relationship between ESG and dividends. Insider parties who prioritize their own interests might prefer to retain cash for personal gain, resulting in lower dividend payouts (Fiorillo & Santilli, 2024). However, our findings reveal the opposite pattern: insider ownership is linked to higher dividends, whereas external ownership is associated with lower dividend distributions. This suggests that insider owners, rather than extracting private benefits, are more likely to overcome agency conflicts with minority shareholders and distribute dividends, potentially motivated by long-term objectives such as maintaining reputation and responding to social concerns. This supports prior studies indicating that high dividends in such firms may serve as a “bonding mechanism” to align interests and signal financial health to minority shareholders (Yilmaz, Aksoy & Khan, 2024; Benlemlih, 2019). Meanwhile, lower dividends in firms with high external ownership may reflect a management strategy of retaining earnings for high-growth opportunities. This finding is consistent with our results in Models Y1 and Y2, where growth and cash holdings are negatively associated with dividends, and insider ownership

has a positive influence on dividend payouts, suggesting that cash is distributed to shareholders rather than being used for managerial self-interest.

Finally, the comparison between dividend payout ratio and dividend yield indicates that ESG impacts are more pronounced on payouts relative to total assets and reflects a firm's internal resources and cash flows, which are influenced by ESG initiatives through operational efficiency, cost savings, higher earnings, and reduced risk exposure (Yang, Liu & Su, 2025; Aydoğmuş, Gülay & Ergun, 2020; Rakotomavo, 2012) than on market-based measures. Dividend yield is sensitive to stock price fluctuations, which may dilute the observable effect of ESG activities, suggesting that the benefits of ESG investments may first manifest in internal financial capacity before being fully reflected in market valuations.

Conclusions, Limitations, and Future Research Lines

This study investigates the relationship between ESG (Environmental, Social, and Governance) performance and dividend payout policies among European firms listed on Euronext between 2019 and 2023. The analysis provides substantial evidence that firms with higher ESG scores continue to pay dividends. At the micro level, the E (Environmental), S (Social), and G (Governance) components reveal unequal impact. This suggests that companies with robust ESG practices, particularly strong governance structures, align better with shareholder interests and are more likely to adopt shareholder-friendly dividend policies. The positive link between ESG performance and dividend payouts challenges the traditional view that high ESG spending requires sacrificing dividends, highlighting those sustainable practices can also lead to financial benefits for shareholders.

One of the central findings of the study is that profitability remains a key determinant of dividend payouts. As expected, firms that are more profitable are better positioned to distribute dividends, as they generate higher free cash flows. This supports the notion that profitability is a key driver of dividend policies, with firms opting to return profits to shareholders when financial conditions permit. On the other hand, firm size and leverage have a negative effect on dividends. Larger firms, due to their size and investment requirements, tend to pay lower dividends, possibly because they prioritize reinvestment over cash distribution. Similarly, firms with higher leverage often face higher financial costs, which reduces their ability to distribute dividends. This finding reinforces the notion that debt serves as a substitute for dividends, a concept supported by prior research.

The study also highlights the role of ownership structure in shaping dividend payout decisions. Insider ownership is positively correlated with higher dividend payouts, suggesting that when managers have a stake in the company, they are more likely to align their interests with those of shareholders and distribute dividends. This result is consistent with agency theory, which argues that insider ownership reduces agency costs by ensuring that managers act in the best interests of shareholders. In contrast, external ownership, particularly external institutional ownership, is negatively related to dividend payouts. This may be because firms with high external ownership are more likely to retain earnings for reinvestment rather than pay out dividends, as institutional investors may prioritize growth over immediate cash returns. Board characteristics also play an important role in the ESG-dividend relationship. Board size is positively correlated with dividend payouts, suggesting that larger boards may be more effective in overseeing management and ensuring that dividend policies align with shareholder interests. This finding underscores the importance of effective corporate governance in promoting shareholder-friendly practices. However, board independence does not show a significant effect on dividends, indicating that simply having independent directors may not be sufficient to influence dividend decisions. This suggests that the quality and engagement of board members may be more important than their independence alone.

Furthermore, the study compares the effects of ESG on dividend payout ratios and dividend yield. It finds that ESG performance has a more pronounced impact on the dividend payout ratio, which reflects a firm's internal capacity to distribute cash, than on dividend yield. This is likely due to the

fact that dividend yield is more sensitive to stock price fluctuations, which can obscure the true effect of ESG practices. In contrast, the dividend payout ratio is more directly influenced by a firm's operational efficiency and cash flow, which can be positively affected by ESG initiatives such as improved risk management and cost savings.

This study has several limitations. Firstly, the sample size could be larger to improve the generalizability of the results. In terms of data limitations, the study relies on secondary data from Refinitiv, which does not cover all relevant companies or industries. Furthermore, the dataset may contain missing or incomplete data for certain variables or years, which could potentially affect the coverage, accuracy, and consistency of the analysis.

Future research could expand this analysis by including other stock exchanges or by differentiating between industries to identify sector-specific ESG impacts on dividend policy, enabling a more comprehensive analysis of how ESG scores influence dividend policies across countries with diverse ownership structures and regulatory frameworks. Additionally, studies could examine the effect of ESG scores on regular dividend payments and the determinants of dividend amounts to better understand the nuances of dividend decision-making in relation to sustainability performance.

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