



Behavioural Finance Perspectives On Esg Investment Decision-Making

Abstract – This study examines the behavioural finance dimensions of Environmental, Social, and Governance (ESG) investment decision-making among individual investors. Drawing on a structured survey of 106 respondents analysed using multiple regression, chi-square tests, ANOVA, and correlation analysis in R 4.2.0, the research investigates how cognitive biases, emotional influences, risk perceptions, and personal value systems shape ESG portfolio allocation decisions. Key findings reveal that value alignment ($\beta = 0.452$, $p < 0.001$) and emotional influence ($\beta = 0.325$, $p < 0.001$) are the strongest behavioural predictors of ESG commitment, jointly explaining 58.47% of variance in portfolio allocation. Risk perception significantly moderates ESG adoption ($\chi^2 = 42.376$, $p = 0.0003$), with novice investors perceiving substantially higher risk than experienced peers. Personal values and ethical motivations emerge as the most consistent drivers: investors with strong value alignment are 3.48 times more likely to hold high ESG allocations (OR = 3.48, $p < 0.001$). These findings challenge purely rational models of investor behaviour and provide actionable insights for asset managers, financial advisors, and policymakers seeking to expand sustainable finance participation.

Keywords: behavioural finance, ESG investing, investment decision-making, cognitive biases, emotional influence, risk perception, personal values, value alignment, ESG portfolio allocation, individual investors, sustainable finance, ethical investing, regression analysis, ANOVA, chi-square test, correlation analysis, investor behaviour.

I. INTRODUCTION

The intersection of behavioural finance and Environmental, Social, and Governance (ESG) investment decision-making has emerged as one of the most fertile and consequential research frontiers in contemporary finance. Traditional financial theory, anchored in the Efficient Market Hypothesis (EMH) and the axiom of rational investor behaviour, has long struggled to account for the empirical irregularities that characterise actual investment decisions. Behavioural finance—pioneered by Kahneman and Tversky (1979), Thaler (1999), and Hirshleifer (2001)—has systematically documented how cognitive biases, emotional heuristics, and social dynamics reshape investment outcomes in ways that depart materially from rational expectations.

ESG investing, once regarded as a niche discipline practised largely by socially conscious retail investors, has undergone a remarkable mainstreaming. Global assets under management with an ESG mandate surpassed USD 35 trillion in 2020 and are estimated to have exceeded USD 40 trillion by 2023, representing more than one third of total professionally managed assets across major markets (Global Sustainable Investment Alliance, 2020). This transformation reflects not merely heightened sensitivity to environmental and societal concerns, but also a growing institutional recognition that ESG factors can exert material influence on long-term financial performance, systemic risk, and capital allocation efficiency.

Despite this dramatic growth, the decision-making processes underlying ESG investment remain only partially understood. Existing scholarship tends to examine ESG from either a purely financial lens—evaluating risk-return characteristics and factor

exposures—or a normative perspective that assumes investors act on well-defined sustainability preferences. Relatively little empirical attention has been paid to the behavioural mechanisms through which psychological biases, emotional responses, social proof, and value-based utilities jointly determine ESG investment behaviour. This study addresses that gap.

1.1 Research Rationale and Significance

The study is motivated by four converging imperatives. First, the scale of ESG capital allocation demands rigorous behavioural analysis: misallocation driven by systematic biases has consequences not only for individual portfolios but for the broader reallocation of capital toward sustainable economic activities. Second, practitioners—asset managers, financial advisors, and ESG product designers—require evidence-based frameworks for understanding client motivation, managing behavioural risk, and designing communication strategies. Third, policymakers and regulators need insight into the behavioural dimensions of ESG market growth to formulate appropriate disclosure standards and investor protection frameworks. Fourth, academically, ESG investing offers a uniquely rich context for examining how value-driven, emotionally salient, and socially influenced decisions interact with conventional financial reasoning.

1.2 Research Objectives

This study pursues five interconnected objectives:

- ▶ To investigate the prevalence of behavioural biases and their influence on ESG investment allocation decisions.
- ▶ To determine whether and how demographic factors moderate investor behaviour in the ESG domain.
- ▶ To examine how risk perception shapes ESG investment commitment across investor experience levels.



- ▶ To measure the impact of emotional and perceptual factors on ESG portfolio decisions.
- ▶ To assess the role of personal values and ethical orientation in driving ESG investment choices.

1.3 Research Hypotheses

H1: Investors' risk perception exerts a significant effect on their ESG investment decisions.

H2: Investor perceptions and emotional factors have a significant and measurable impact on ESG investment decisions.

H3: Personal values and ethical considerations significantly influence the choice of ESG investments among individual investors.

II. REVIEW OF LITERATURE

The scholarly investigation of ESG investment behaviour has expanded considerably since 2020, producing a substantive body of evidence on the psychological, institutional, and informational determinants of sustainable investing choices. This review synthesises key contributions organised thematically.

2.1 Behavioural Biases in ESG Decision-Making

Amgain (2024), employing a systematic PRISMA review spanning 2013–2023, identified thirty-five distinct psychological biases influencing ESG decision-making, with herding, anchoring, and loss aversion among the most prevalent. Adwani (2024) extended this analysis to emerging market contexts, documenting how cultural norms and entrenched heuristics slow ESG adoption in developing economies and advocating for culturally tailored investor education programmes.

Gupta (2024) provided experimental evidence that herd behaviour and overconfidence impair portfolio diversification in socially responsible investment contexts, calling for structured debiasing interventions. Shu (2025) synthesised findings across multiple studies, highlighting cognitive dissonance and emotional attachment as recurrent psychological drivers, while noting a significant gap in longitudinal empirical research. Ding (2025) drew sharp distinctions between institutional and retail investor bias profiles: retail participants exhibited pronounced overconfidence and loss aversion, whereas institutional counterparts were more susceptible to peer benchmarking and herding dynamics.

Bhatia et al. (2021) demonstrated that overconfidence leads to excessive trading in ESG securities while loss aversion causes investors to retain underperforming sustainable assets beyond what is financially optimal—a finding with direct implications for portfolio efficiency. Shefrin (2024) formalised these dynamics within an extended portfolio theory framework, arguing that psychological preferences and emotional valuations consistently outweigh pure risk-return calculations in ESG contexts.

2.2 Values, Ethics, and Investor Motivation

A distinct strand of literature foregrounds value-based utility as a primary driver of ESG investment. Riedl and Smeets (2017) demonstrated that investors hold socially responsible funds largely on normative grounds, accepting below-market returns in exchange for value alignment. Nilsson (2008) found that pro-social attitudes independently predict ESG allocation beyond financial performance expectations. Garamvolgy (2021) challenged the conventional assumption of a financial trade-off in ESG investing, showing that investors with strong environmental consciousness do not perceive ESG as return-diminishing.

Risi et al. (2021) extended the analysis to organisational behaviour, documenting how managerial values and corporate culture shape the authenticity of ESG implementation. Camilleri (2021) identified gaps between stated ESG commitments and actual behaviour, attributing them to moral self-licensing and impression management dynamics.

2.3 Risk Perception and Information Processing

Zheng (2024) demonstrated that enhanced ESG transparency materially reduces cognitive uncertainty and shifts retail and institutional allocation patterns. Vu (2025) found that ESG stocks exhibit modest underperformance attributable partly to behavioural over-optimism amplified by media attention. Vanwalleghem (2021) documented sentiment-driven pricing inefficiencies in ESG securities, where attention bias and emotional trading create mispricing that sophisticated investors can exploit.

Heinkel et al. (2021) showed that investor preferences shaped by social norms and ethical concerns create market segmentation, raising the cost of capital for firms with poor ESG profiles. Busch et al. (2021) extended this to institutional contexts, identifying reputational contagion and competitive mimicry as structural accelerants of ESG adoption across the asset management industry.

2.4 Demographic and Institutional Determinants

Kumar and Sharma (2024) identified significant gender-based heterogeneity in ESG decision-making within Indian markets, with women investors demonstrating differential responsiveness to social performance metrics. Thapa (2024) demonstrated that growing institutional ownership systematically reduces future ESG misconduct in portfolio firms, underlining the governance channel through which behavioural forces shape corporate outcomes. Abideen et al. (2023) provided cross-market evidence that herd behaviour, anchoring, and overconfidence affect ESG product adoption rates, with implications for investor education design.

III. RESEARCH METHODOLOGY



An Empirical Investigation of Cognitive Biases, Emotional Drivers, and Value Alignment

Field	Details
Research Type	Empirical Behavioural Finance
Domain	Sustainable Investing / ESG
Sample Size	N = 106 Investors
Methodology	Survey Regression Chi-Square ANOVA Correlation
Analysis Software	R 4.2.0 ($\alpha = 0.05$)
Year	2026

3.1 Research Design

This study adopts a cross-sectional, quantitative research design underpinned by a primary survey instrument. The approach is appropriate for capturing the distributional properties of behavioural variables across a heterogeneous investor sample and for testing hypothesised relationships through inferential statistics.

3.2 Sample Design and Data Collection

A purposive sampling strategy was employed to ensure meaningful representation across investor experience levels, portfolio size brackets, and age cohorts. Data were collected via structured questionnaires administered in both digital (survey link) and physical formats to individual investors actively engaged in financial markets. The final analytical sample comprised 106 respondents (N = 106), after removing incomplete responses. This sample size is appropriate for an exploratory empirical study and satisfies the minimum-30-per-subgroup threshold for the inferential tests applied.

3.3 Instrument Design

The survey instrument comprised 30 items organised across seven sections: (A) demographic profile, (B) ESG awareness and attitudes, (C) behavioural decision-making patterns, (D) risk perception, (E) information processing, (F) additional behavioural motivators, and (G) cognitive bias self-assessment. Items in Sections B–G employed five-point Likert-type scales. Sections C and E included categorical items capturing decision typologies and information source preferences. The questionnaire operationalised five primary constructs: behavioural biases (overconfidence, herding, confirmation bias, framing, value alignment), risk perception, emotional influence, personal values and ethics, and ESG allocation commitment.

3.4 Analytical Methods

All analyses were conducted in R 4.2.0 at a significance threshold of $\alpha = 0.05$. The following techniques were applied:

Statistical Method	Objective	Purpose
Multiple Regression (OLS)	1, 4	Predict ESG allocation from behavioural predictors
Spearman Rank Correlation	2	Experience vs. ESG behaviour
Chi-Square Tests	3, 4, 5	Association between categorical variables
One-way ANOVA	3	Risk perception across experience levels
Correlation Matrix	3, 5	Multi-dimensional relationship mapping
Logistic Regression	5	Predict high vs. low ESG allocation

3.5 Scope and Limitations

The study spans retail, intermediate, and advanced individual investors primarily in the Indian market context. Limitations include potential social desirability bias in self-reported commitment to ESG, the cross-sectional nature of data collection precluding causal inference, and sample constraints that may limit generalisability to ultra-high-net-worth and institutional investor segments. The dynamic evolution of ESG regulatory standards and rating methodologies also means findings should be interpreted in the context of 2024–2025 market conditions.

IV. RESULTS AND ANALYSIS

4.1 Demographic Profile of Respondents

The sample skewed toward younger, professionally active investors: the modal age cohort was 30–39 years (31.1%), followed by 20–29 years (26.4%), reflecting millennial dominance in ESG market participation. Investment experience was primarily intermediate (39.6%), with a mean experience score of 2.41 (SD = 0.95) on a four-point scale from Beginner to Expert. Portfolio values were concentrated in the ₹50,000–₹500,000 range (35.8%), with meaningful representation across higher wealth brackets, producing a sample with a retail-dominant but financially substantive composition.



4.2 Objective 1 — Behavioural Biases and ESG Allocation
Descriptive Analysis of Bias Constructs

Behavioural Construct	Mean (1–5)	SD	Interpretation
Value Alignment	3.89	0.82	Strongest bias — dominant driver
Framing Effects	3.61	0.91	High sensitivity to presentation
Emotional Influence	3.47	0.98	Significant emotional overlay
Herding Behaviour	3.12	1.15	High variance — heterogeneous response
Overconfidence	2.54	1.03	Weakest bias — investor scepticism

Multiple Regression Analysis

The OLS regression model with portfolio ESG allocation as the dependent variable and six behavioural predictors yielded a robust fit:

Predictor	β Coefficient	Std. Error	t-value	p-value
Value Alignment	0.452	0.089	5.08	< 0.001 ***
Emotional Influence	0.325	0.094	3.46	< 0.001 ***
Framing Effects	0.218	0.087	2.51	0.014 *
Herding Behaviour	0.176	0.091	1.93	0.046 *
Loss Aversion	0.154	0.083	1.86	0.042 *

Overconfidence	0.098	0.079	1.24	0.217
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Model Summary: $R^2 = 0.5847$ | Adjusted $R^2 = 0.5595$ | $F(6, 99) = 23.21, p < 0.001$ | All VIF < 3.0 (no multicollinearity)

The model explained 58.47% of variance in ESG allocation—a high explanatory power for a behavioural construct. Value alignment ($\beta = 0.452$) was the dominant predictor, followed by emotional influence ($\beta = 0.325$). All biases except overconfidence reached statistical significance, confirming that psychological factors play a pervasive role in ESG investment decisions beyond what traditional rational-choice frameworks would predict.

4.3 Objective 2 — Demographic Moderators of ESG Behaviour

Spearman rank correlations between investment experience and ESG behavioural indices were uniformly positive and statistically significant: ESG awareness ($\rho = 0.42, p < 0.001$), portfolio allocation ($\rho = 0.38, p < 0.001$), and perceived risk ($\rho = -0.45, p < 0.001$). More experienced investors report lower perceived ESG risk, greater ESG awareness, and higher allocation rates, consistent with a learning-by-doing mechanism that reduces psychological barriers over time.

Portfolio value also correlated positively with ESG allocation, suggesting that wealth acts as both a financial enabler and a psychological precondition for values-based investing. Governance awareness was uniformly high across age cohorts (mean range: 3.6–3.9), but allocation behaviour varied significantly, indicating that awareness alone does not translate into commitment without the joint presence of financial capacity and values orientation.

4.4 Objective 3 — Risk Perception and ESG

Commitment Chi-Square Analysis

A Pearson chi-square test revealed a statistically significant association between risk perception category and ESG portfolio allocation tier ($\chi^2 = 42.376, df = 16, p = 0.0003$; Cramer's $V = 0.316$, medium effect size). Among respondents perceiving ESG as lower risk (26.4%), the majority allocated more than 25% of their portfolio to ESG assets. Conversely, among those perceiving higher risk (34.9%), ESG allocation was predominantly below 10%, with 38.7% perceiving ESG risk as equivalent to traditional investments.

ANOVA Across Experience Levels

One-way ANOVA confirmed that risk perception scores differed significantly across the four investment experience categories ($F = 7.823, df = 3/102, p < 0.001, \eta^2 = 0.187$). Post-hoc analysis revealed that Beginners reported substantially higher perceived ESG risk than



Intermediate, Advanced, and Expert investors. This monotonic decline in risk perception with experience underscores the role of investor education and market familiarity in lowering psychological entry barriers.

Correlation analysis further confirmed that risk perception was negatively associated with all ESG factor dimensions: environmental factors ($r = -0.312$), social factors ($r = -0.278$), governance factors ($r = -0.245$), and most strongly, value alignment ($r = -0.398$, $p < 0.001$). These converging findings support H1: risk perception is a significant and consistent determinant of ESG investment behaviour.

4.5 Objective 4 — Emotional and Perceptual Drivers of ESG Decisions

Chi-square analysis of emotional decision style against ESG allocation patterns ($\chi^2 = 38.542$, $df = 12$, $p = 0.0001$; Cramer's $V = 0.348$) revealed a medium-large effect: investors adopting a balanced emotional-rational approach displayed the strongest positive correlation with ESG allocation ($r = 0.512$), while purely rational investors exhibited a negative association ($r = -0.423$). Highly emotional investors also showed above-average ESG commitment ($r = 0.387$).

Multiple regression of perception variables on ESG allocation corroborated these results. ESG impact belief ($\beta = 0.389$, $p < 0.001$) and ESG performance perception ($\beta = 0.312$, $p < 0.001$) were the strongest perceptual predictors. These findings directly challenge the canonical assumption of emotion-free rational decision-making in finance, establishing that emotional engagement—when paired with analytical consideration—enhances rather than undermines sustainable investment commitment. H2 is accepted.

4.6 Objective 5 — Personal Values, Ethics, and ESG Choices

The chi-square test comparing values conflict resolution patterns with primary ESG motivation produced the largest effect size of all hypotheses tested ($\chi^2 = 56.743$, $df = 20$, $p < 0.001$; Cramer's $V = 0.411$). Among surveyed investors, 58.4% reported always or usually prioritising personal values over financial returns when values conflict arose. Ethical considerations were cited as the primary motivation by 39.6% of respondents.

Logistic Regression Model

Predictor	Odds Ratio	Std. Error	z-value	p-value
Value Alignment	3.484	0.423	7.32	< 0.001 ***
Ethical Motivation	2.671	0.387	4.89	< 0.001 ***

Values Priority	2.150	0.356	3.71	0.0018 **
Income Level	1.408	0.241	2.19	0.029*
Age Group	1.182	0.218	1.73	0.0839

Model Fit: Classification Accuracy = 76.4% | Sensitivity = 71.2% | Specificity = 79.8% | AIC = 99.56

Value-aligned investors are 3.48 times more likely to maintain high ESG allocations (>25% of portfolio). Ethical motivation and values priority independently increased the odds of high ESG allocation by factors of 2.67 and 2.15 respectively. Correlation analysis confirmed that value dimensions align tightly with corresponding ESG factor categories: governance ethics and governance factors ($r = 0.812$), environmental values and environmental factors ($r = 0.789$), social justice values and social factors ($r = 0.734$). H3 is accepted with the highest empirical support of the three hypotheses.

V. DISCUSSION

5.1 The Primacy of Value-Based Utility

The dominant finding of this study—that personal value alignment is the strongest, most consistent predictor of ESG investment behaviour—challenges the prevailing finance paradigm in which investor utility is reducible to risk-return optimisation. Our results are consistent with Riedl and Smeets (2017) in confirming that investors derive non-financial utility from value alignment. The magnitude of the effect ($OR = 3.48$; $\beta = 0.452$) suggests that this utility is not merely supplementary but constitutive of ESG investment motivation for a substantial proportion of individual investors.

The tight coupling between investors' personal value dimensions and their emphasis on corresponding ESG factor categories (all $r > 0.73$, $p < 0.001$) implies that ESG investing, at the individual level, functions less as a financial strategy than as a values-expression mechanism. This has profound implications for how ESG products are designed, marketed, and communicated: appeals to values authenticity and mission alignment are likely to be more effective than purely performance-based arguments.

5.2 The Constructive Role of Emotion in Sustainable Investing

The finding that purely rational investors exhibit a negative association with ESG allocation ($r = -0.423$), while investors combining emotional engagement with analytical discipline show the strongest positive association ($r = 0.512$), represents a direct empirical challenge to the rationalist canon. Rather than distorting investment decisions, emotional engagement with sustainability themes appears to activate pro-social



preferences and maintain commitment in the face of short-term performance volatility.

This is consistent with the warm-glow utility framework (Andreoni, 1990) and with Shefrin (2024), who argues that psychological preferences represent legitimate utility components rather than cognitive errors to be eliminated. From a practical standpoint, it suggests that effective ESG advisory relationships should legitimately incorporate values dialogue and emotional resonance alongside conventional financial analysis.

5.3 Risk Perception as a Structural Barrier

The systematic elevation of perceived risk among novice investors (ANOVA, $F = 7.823$, $p < 0.001$) identifies risk misperception as a principal structural barrier to ESG market broadening. Since actual ESG risk-return profiles are broadly neutral to positive across time horizons (Friede et al., 2015; Morningstar 2020 analysis), the elevated risk perceptions among beginners reflect an informational and experiential deficit rather than a fundamental characteristic of ESG assets.

The implication is that targeted investor education, standardised ESG performance disclosure, and accessible risk-adjusted return benchmarks could significantly accelerate ESG adoption among inexperienced investor segments—which represent a large and growing share of the global investor base.

5.4 Framing, Information Architecture, and Behavioural Design

The significant coefficient for framing effects ($\beta = 0.218$, $p = 0.014$) confirms that the manner in which ESG information is presented materially influences investment decisions. ESG reporting remains fragmented, with multiple competing rating methodologies and disclosure formats generating cognitive load that may discourage engagement. Design interventions that simplify ESG metrics, emphasise impact narratives, and use value-consistent language could reduce anchoring and representativeness biases, consistent with recommendations by Ravnish (2025) and Zheng (2024).

VI. CONCLUSION AND RECOMMENDATIONS

6.1 Summary of Findings

This study offers a systematic empirical account of the behavioural architecture of ESG investment decision-making. Three convergent conclusions emerge:

- ▶ ESG investing is fundamentally a values-driven behaviour: personal value alignment is the dominant predictor of ESG allocation ($\beta = 0.452$, $OR = 3.48$), and its influence surpasses conventional financial variables in explanatory power within the behavioural model.

- ▶ Emotion is a constructive, not disruptive, force in ESG investment: a balanced emotional-rational decision style produces the highest ESG commitment. Purely rational framings suppress ESG allocation, suggesting that ESG finance requires emotionally intelligent advisory and communication models.

- ▶ Risk perception is the primary structural barrier to ESG adoption: novice investors systematically overestimate ESG risk, and investment experience monotonically reduces this misperception, confirming that education and transparency are the most powerful regulatory and market-development levers.

All three research hypotheses are accepted. The behavioural regression model explains 58.47% of variance in ESG allocation, providing a robust empirical foundation for the theoretical and practical contributions claimed.

6.2 Implications

For Asset Managers and Financial Advisors

Client segmentation and communication strategies should explicitly incorporate values profiling alongside conventional risk profiling. ESG product narratives that resonate with identified value preferences—environmental, social, or governance—will produce stronger and more durable investor commitment than return-focused communications alone. Debiasing tools should target risk misperception among novice investors, while advanced investors may benefit from diversification coaching to address herding risks.

For Regulators and Policymakers

Disclosure frameworks should prioritise standardisation, simplicity, and risk-adjusted comparability to reduce cognitive barriers and enable accurate risk perception. Mandatory ESG literacy components in investor education programmes, particularly for retail investor onboarding, could materially reduce the experience-dependent risk misperception documented in this study. India's SEBI BRSR framework and its expansion to supply chain disclosures represent positive steps that the international regulatory community could adopt as a model.

6.3 Directions for Future Research

- ▶ Longitudinal designs tracking investor ESG behaviour across market cycles would enable causal inference and document how learning dynamics reduce behavioural barriers over time.

- ▶ Cross-cultural comparative studies are needed to assess whether the primacy of value alignment is culturally universal or moderated by national institutional contexts.

- ▶ The impact of AI-driven ESG analytics tools on bias reduction and decision quality merits dedicated experimental investigation.

- ▶ Integration of physiological and neurological measures (e.g., galvanic skin response, eye-tracking) in laboratory settings could provide objective validation of self-reported emotional influence findings.



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