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Original Paper

Institutional Investor Shareholdings and Corporate Sustainability: A Study from the Perspective of Corporate Governance

Mingxuan Cao[1]

[1] University of Alberta, Edmonton, Alberta, Canada

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Abstract

This research analyzes how institutional investors' holdings of shares impact enterprises' sustainability-development activity as facilitated by corporate governance systems between investors and other stakeholders. Using agency theory and stakeholder theory, an analytical framework was developed by the authors to examine the various pathways that institutional investors (IIs) exercise their oversight responsibilities in addition to their strategic roles. The authors state that embedding environmental, social, and governance (ESG) measures into executive-incentive agreements can significantly improve corporate performance, and active ownership practices of IIs combined with synergy from other IIs also provide an important foundation for these measures. The researchers conclude that the construction of a governance ecosystem that is based upon long-term value is central to promoting sustainable development through institutional capital.

Keywords

Institutional Investors, Corporate Sustainability, ESG Performance, Corporate Governance, Executive Incentives, Oversight Mechanisms

1. Introduction

Institutional investors play a vital role in the ownership of companies and in their governance decisions. Their investment patterns influence how management engages with shareholders, which ultimately determines how a company develops over time. Sustainability is no longer limited to the financial bottom line; it includes environmental and social considerations as part of corporate strategies. Therefore, corporate governance models face new challenges in regard to the inclusion of sustainability in corporate business plans. To support these new challenges, institutional investors have provided new ways for companies to include sustainability in their operations. Institutional investors provide capital and may also participate in the governance of an organization through the exercise of their voting rights; by providing communication and dialogue with management; and by designing incentive structures that reward companies for developing sustainable practices. By exploring how institutional investors can leverage their governance tools to turn the pressures of sustainable development into corporate action, researchers can gain insights into the relationship between capital markets and industry today, and identify ways to optimise the functioning of capital markets to support the real economy.

2. Theoretical Foundation: The Mechanism by Which Institutional Investors Influence Corporate Sustainable Development

2.1 Conceptual Definitions: Types and Behavioral Characteristics of Institutional Investors, the Connotation of Corporate Sustainable Development (ESG)

Large institutional investors generally refer to organisations that manage investments based on the authority granted by legal contractual agreements with name brands of finance. A majority of large institutional investors utilize long-term strategies versus trading strategies when making investment decisions and will ultimately influence the performance of a company through the exercise of their voting rights, communication with boards of directors, and by focusing on the company's management of strategic business issues. Sustainable development is often defined by three major categories: (i) Environmental issues; (ii) Social issues and (iii) Corporate governance issues. The ‘Environmental’ category refers to how a company uses its resources and how its resource consumption affects the environment; the ‘Social’ category includes how the company treats its employees and how it interacts with the surrounding community, i.e., the company’s interaction with its local and global stakeholders; whereas the ‘Corporate Governance’ category focuses primarily on a company’s ability to make sound decisions regarding the management and governance of the company and the separation of powers between the various levels of management. By linking capital allocation and decision-making levels of a company to issues relating to environmental, social, and corporate governance, the market expects an organisation to effectively manage long-term risks and determine how capital is allocated over the long-term (Zhang, X. H., Zhao, J. Q., & Zhang, Y., 2024).

2.2 Theoretical Framework: Principal-Agent and Oversight Functions, Stakeholders and Value Co-Creation, Resource Dependence and Strategic Impact

The agency theory describes the potential for varied objectives to occur among both the owners (shareholders) of a company and those charged with managing the company (executives). Institutional investors that control a large amount of stock in a firm can assist in resolving or at least reducing, such agency conflicts by assuming the supervisory role of corporate managements, compelling them into a more significant focus on the long-term effects of their actions on the environment, society, and other interested stakeholders (broadly defined). Stakeholder theory provides a framework for understanding how this action is larger than just the maximization of shareholder value, as it supports the view that corporate value is achieved through a business's relationships and collaboration with many different groups of stakeholders, including but not limited to employees, consumers, and communities. The ability of institutional investors to manage and control many of the company's resources increases the level of strategic influence that institutional investors have over a company's strategic decision-making. In addition to providing capital to companies, institutional investors provide developers and businesses with the assurance of the institutional investor's market reputational resources. The combination of these two resources provides institutional investors with the opportunity to be engaged in an ongoing dialogue with the firms they support regarding the sustainable development strategies of those firms.

3. Real-world Challenges: The Struggle of Institutional Investors to Drive Sustainable Development

3.1 The Conflict Between Short-Term Return Pressures and Long-Term ESG Investing

Many institutional investors themselves are also in a complex entrusted chain, with their funds coming from pension or insurance clients seeking regular returns. This entrusted responsibility anchors investors' focus on quarterly or annual financial performance. The commonly used relative performance ranking mechanism in the market further amplifies short-term comparative pressure, making investment managers prioritize financial decisions that can quickly boost stock prices when allocating capital, while often lacking sufficient patience for environmental or social projects that are beneficial to the long-term resilience and brand reputation of the enterprise but have insignificant short-term financial returns. The investment of enterprises in emission reduction technology research and development, supply chain social responsibility audits, or employee skill transformation usually takes several years to gradually translate into measurable cost savings, risk reduction, or revenue growth. This return cycle is fundamentally mismatched with the performance evaluation cycle of most institutional investors on an annual or even quarterly basis. The adjustment of investment strategies has become exceptionally cautious as a result. Even if the investment team agrees with the long-term value of sustainable development issues in their philosophy, under the existing incentive mechanism, they may choose to maintain their focus on traditional financial indicators due to concerns about lagging short-term performance, thereby continuing capital support for existing high carbon or highly controversial business models (Yan, 2011).

3.2 The Lack of Standardized ESG Metrics and the Challenge of Executive Incentive Design

A key barrier to the integration of sustainability-related factors into executive remuneration today is the continuous absence of any uniform definition or standard for evaluating these factors. Due to the large variation in the performance metrics selected by various companies and/or industry groups, it is difficult to compare performance on an equitable basis across industries and to assess the relative achievement of its sustainability goals. For example, as an energy company, Exxon Mobil links executive compensation to specific greenhouse gas emissions intensity targets that are reflective of the direct environmental impact of their operations. In contrast, as a technology company, Hewlett Packard ties its leadership bonuses to measures of success for women in executive positions. On the other hand, Chevron, an industrial company, ties both safety performance and gas flaring reduction to its compensation incentives, thus exemplifying the challenges of aligning the issues of social safety with those of environmental performance. The result of this disparity between simultaneous acceptance of diverse performance metrics is the inherent difficulty in creating an overall system that can be uniformly applied across companies, making it difficult for investors and others to determine the legitimacy of sustainability commitments made by various businesses.

3.3 The Surface-Level Nature of ESG Information Disclosure and the Risk of Communication Distortion

Various companies release ESG Reports which are made to accentuate the positive things that companies are doing with regards to ESG and downplay any actual challenges that may exist. The result is that the ESG report does not accurately depict the reality of the company's operations and creates distance between the content of the report and the actual complexity of the previously mentioned operations. There is also a tendency for many of the reporting frameworks to focus on those indicators that are the easiest to collect and compile, while the indicators that are more challenging to compile, such as the long-term social impacts or deeper supply chain risks for example, are likely to be oversimplified by the reporting framework. These filtered indicators create an incomplete view of the true environmental and social risks facing a company, and therefore make it difficult for investors to accurately gauge how prepared a company is for long-term sustainable development. As such the challenge of distorted communication erodes the credibility of the report. Additionally, it is difficult to differentiate the substantive differences between various companies' action plans, as well as the degree of execution intensity, when multiple companies use the same standardized verbiage in their reports when describing their sustainable development commitments. Finally, the demand for transparent and verifiable information continues to increase in the market place, which is in contrast to the trend of superficiality found in numerous ESG reports today. Consequently, it has become extremely difficult for institutional investors to be able to engage in a thorough analysis and to provide effective governance due to this trend (Cai, Zhou, & Xie, 2026).

3.4 Heterogeneous Institutional Motivation Differentiation and Insufficient Governance Participation Effectiveness

The composition of institutional investors is inherently diverse, with pension funds and insurance companies typically having a longer-term perspective on debt matching, while hedge funds or some mutual funds may be more focused on trading opportunities brought about by short-term market fluctuations. The difference in intrinsic motivation directly affects their level of investment and participation in sustainable development issues for enterprises. Long term oriented investors may be willing to engage in years of in-depth communication to drive companies to improve their environmental management, while transactional investors tend to make buying and selling decisions quickly rather than participating in lengthy governance processes. Even among long-term investors, there are differences in the judgment of which ESG issues are financially important, with some focusing on environmental risks such as climate change, while others are more concerned with labor rights or corporate ethics. The differentiation of motives makes it difficult to form a stable and unified action alliance when exercising shareholder rights, weakening the collective ability of shareholders to transmit clear and strong reform signals to the management of the enterprise, and making the external governance supervision that should have been effective fragmented and inefficient.

3.5 The Transmission Blockage of Internal Governance Structure on External Influence

The internal power structure of a company sometimes forms an intangible barrier to external shareholders' suggestions, and the concentration of equity in founders or related parties may weaken the discourse space of other investors in major decisions. If the selection of board members does not fully reflect independence, the decision-making process may be more inclined to maintain the preferences of the existing management rather than responding to the demands of a wide range of shareholders. Even if institutional investors successfully propose improvement suggestions regarding environmental or social risks, these opinions may be delayed or diluted when conveyed to specific executing departments due to unclear division of responsibilities or conflicting performance goals of middle-level managers. If the compensation incentives of the management themselves are still mainly tied to short-term financial indicators, then the long-term sustainable development pressure from external shareholders will be difficult to translate into actual resource allocation and operational changes. These inherent structural and incentive factors in the internal governance mechanism make external influence face numerous filters and losses when penetrating into the daily operations of enterprises.

4. Governance Path: Strategies to Strengthen Institutional Investors in Promoting Sustainable Development

4.1 Internal Governance Enhancement: Establishing an ESG-oriented Executive Incentive and Board Oversight Mechanism

The optimization of internal corporate governance structures requires translating abstract sustainability goals into specific metrics that directly impact executive compensation. For instance, ExxonMobil explicitly links executive bonuses to greenhouse gas emission reduction progress, compelling management to weigh environmental impacts in operational decisions. HP ties leadership pay to targets for increasing the proportion of female executives, ensuring tangible resource support for diversity commitments in talent development. Chevron incorporates both safety performance records and gas flaring control objectives into its incentive programs, demonstrating the feasibility of integrating operational risks with social and environmental accountability in performance evaluations. These practices collectively reveal that well-designed performance metrics can effectively convert external pressures into internal management drivers. Meanwhile, boards must assume a more critical oversight role by establishing dedicated committees or enhancing existing audit functions to continuously review the scientific validity of these non-financial metrics, data collection reliability, and the seriousness of final compensation 兑现. This creates a comprehensive internal governance loop—from goal setting to execution supervision—ensuring sustainability is no longer confined to reporting commitments but embedded in core decision-making processes (Minev, Dankova, & Štrukelj, 2025).

4.2 Enhancing Investor Capabilities: Deepening ESG Integration, Active Ownership, and Diligent Management Practices

Institutional investors must go beyond merely treating ESG factors as labels for investment screening and instead develop systematic internal capabilities to assess the actual impact of these non-financial issues on a company's long-term value. This requires investment teams to be staffed with professionals specializing in environmental science, social policy, or corporate governance, enabling in-depth analysis of specific sustainability risks and opportunities faced by enterprises. In the case of ExxonMobil, the investors driving its pay reform did not simply voice generalized concerns but instead proposed concrete solutions to tie emission reduction targets to executive incentives, based on professional evaluations of the financial implications of climate risks. Such rigorous ESG stewardship demands sustained, high-quality engagement from investors, leveraging shareholder rights to participate in corporate governance discussions and even submitting shareholder proposals to advance specific reforms. The enhancement of capabilities is also reflected in voting decisions, where institutional investors must exercise voting rights based on independent analysis of each company's ESG performance and risks, rather than relying on uniform templates, thereby precisely channeling capital guidance toward the governance areas with the greatest potential for improvement.

4.3 External Institutional Synergy: Promoting the Integration of Information Disclosure, Rating Standards, and Regulatory Policies

Institutional investors need to go beyond simply using ESG factors as investment screening labels and instead establish a systematic internal capability to assess the actual impact of these non-financial issues on the long-term value of the company. This means that the investment team must be equipped with professionals with expertise in environmental science, social policy, or corporate governance who can interpret the economic implications of a company's carbon emission path, assess potential operational and reputational risks posed by supply chain labor practices, or analyze the true impact of board diversity on the quality of company decision-making. For example, in the case of ExxonMobil, investors driving its compensation reform not only expressed concerns, but also relied on internal climate analysis models to demonstrate the potential impact of transformation risks on the company's asset value, and proposed specific technical solutions that link emission reduction targets with executive incentives. This in-depth and responsible management practice requires investors to engage in continuous professional interaction, including regular meetings with the company's management and board of directors, detailed inquiries about monitoring data of its environmental management system or improvement schedules for social issues, and even, when necessary, joint submission of finely crafted legal proposals with other shareholders to promote governance structure reform (Dossa, Gopang, Thomas et al., 2025). The improvement of capabilities ultimately needs to be reflected in the quality of voting decisions. Institutional investors need to exercise their voting rights based on independent analysis of each company's ESG performance, such as carefully judging whether a company's greenhouse gas emission reduction targets have sufficient ambition and scientific implementation paths, rather than relying on a unified voting guide, so as to accurately apply the guiding role of capital to the governance links with the most substantial improvement potential.

4.4 Long-term Ecological Construction: Advocating Patient Capital and Strengthening Multi-party Dialogue and Value Consensus

The transformation of the value orientation of the capital market towards the long-term dimension relies on the systematic advocacy of the concept of patient capital and the construction of an ecosystem that can nourish this concept. As the source of capital, asset owners such as pension funds and insurance funds should first adjust their requirements for entrusting asset management institutions and clearly include long-term sustainable development results in the performance evaluation system. Asset management institutions can reform their internal incentive mechanisms accordingly, explore extending the assessment period for investment managers, and design reward schemes that link the successful completion of key ESG transformations by invested companies with team compensation. Enterprises themselves need to break through the traditional investor relations management model and establish exclusive channels for regular and forward-looking dialogue with long-term shareholders. For example, a sustainable development committee led by independent directors should be established to regularly meet with core investors and deeply explore strategic issues that require long-term investment, such as technological transformation paths and supply chain risk management. Cross industry advocacy organizations and professional platforms can play a unique neutral coordinating role, convening investors, business managers, policy researchers, and community representatives from different fields to jointly discuss practical and feasible transition paths and cooperation frameworks for specific challenges such as decarbonization of heavy industry and inclusive growth of the digital economy. The continuous research in academia and independent think tanks, especially the empirical tracking of the dynamic relationship between long-term ESG factors and financial performance, can provide an indispensable evidence basis and conceptual framework for all the above practices, helping market parties to go beyond short-term disputes on complex issues and gather substantive consensus on the long-term value connotation (Srairi, 2025).

4.5 Technology Empowerment in Governance: Leveraging Fintech to Enhance Data Transparency and Analytical Efficiency

Financial technology development allows us to use advanced technology tools to solve the challenges associated with the quality and reliability of ESG data. Blockchain technology can be used to create a data authentication system that allows tracking the original source of key environmental and social indicators to ensure data integrity and that it remains unchanged during transmission and aggregation. By using AI-based algorithms at scale and specifically natural language processing technologies, investors can more effectively review and assess the multitude of unstructured reports produced by companies while identifying both potential indicators of risk as well as information that may be contradictory to one another. The availability of a shared platform for ESG data reporting will significantly reduce the cost of compliance of enterprises preparing ESG disclosure data while also increasing the comparability of the data between companies. Additionally, these data analysis tools will enable institutional investors to correlate large amounts of ESG data produced by companies against other data such as the company's financial performance, supply chain map, and even the geographic location of the asset to more definitively assess the impact that various types of environmental risk will have on the value of a company's asset. Technology empowerment ultimately serves wiser decision-making. When investors can easily access more reliable, timely, and in-depth sustainable development information, their voting decisions and responsible management activities may be based on a more solid factual foundation, making the guiding role of capital towards goodness more precise and effective (Shang, Song, Yu et al., 2025).

5. Conclusion

As a way of introducing new drivers and factors around enterprise sustainable development, Institutional Investors combine their position as shareholders with their role as unique shareholders involved in corporate governance. This helps to illustrate the importance of developing several governance mechanisms to align short-term pressures in the market with the potential for long-term value creation. For future research, it will be important to conduct a more extensive examination of institutional investors (and their different types) with a focus on the impact of institutional background, stability during periods of market volatility, and certain characteristics that distinguish different types of institutional investors. The success of enterprises' paths towards sustainable development through institutional investor consensus depends not only on the convergence of consensus around value at all levels but also on the establishment of strong resilience in governance to withstand cyclical fluctuations and multiple indicators. This represents, in many ways, the ultimate expression of capital's quest for good.

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