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Role of ESG-based incentives in fostering workforce engagement

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Abstract
This study investigates the role of Environmental, Social, and Governance (ESG)-based incentives in fostering employee engagement and retention within modern organizations. As organizations increasingly embed sustainability goals into their operational frameworks, aligning employee compensation with ESG objectives has emerged as a promising strategy to enhance motivation and long-term commitment. Using a mixed-methods approach, the research assesses employee perceptions and engagement levels associated with ESG-linked rewards. Primary data were collected from 30 employees across different companies in Info Park Cochin, with statistical tools such as regression analysis and mean score evaluations employed to interpret the data. Findings indicate a strong positive correlation between ESG-based incentives and employee engagement, with 42% of the variance in engagement explained by the inclusion of ESG-focused compensation. Social and governance practices, particularly anti-corruption policies, diversity, and inclusion initiatives, were highly valued by employees. The study highlights the growing preference for meaningful, value-aligned work environments and suggests that ESG-integrated reward systems serve as effective levers for enhancing workplace culture, motivation, and loyalty. The research contributes to the discourse on sustainable human resource management by offering actionable insights into the design of ESG-informed compensation frameworks.

Keywords: ESG-based incentives, employee engagement, sustainable compensation, corporate governance, workforce retention, employee motivation, environmental sustainability

Introduction

Traditional remuneration strategies often fail to capture the intrinsic value of sustainable practices, thereby missing an opportunity to motivate employees to contribute to long-term corporate objectives. By linking rewards to measurable sustainability targets such as reducing carbon emissions, fostering diversity and inclusion, and ensuring ethical governance organizations are creating a direct connection between individual contributions and the company's overall commitment to sustainable development. This alignment not only reinforces the corporate mission but also resonates with employees who increasingly seek meaningful work that contributes to the greater good.

ESG-based incentives have the potential to reshape workplace culture by fostering a sense of shared purpose and collective responsibility. When employees see their efforts contributing to significant environmental and social improvements, their engagement levels tend to rise, leading to enhanced productivity and innovation. Moreover, a transparent and value-driven compensation structure can strengthen loyalty, as employees are more likely to remain with organizations that consistently demonstrate commitment to sustainable practices. Such loyalty not only reduces turnover-related costs but also preserves institutional knowledge, ultimately bolstering the company's competitive edge. Ajay, R., Jory, S. R., & Syamraj, K. P. (2024) [1] in their research reveals that business-group affiliated firms with higher ESG scores tend to have higher executive compensation than non-affiliated firms. Moreover, environmentally sensitive firms with higher governance pillar scores, which represent better governance practices, show higher executive compensation. Finally, high ESG scores and executive compensation is associated with better firm performance.

Despite the promising benefits, empirical research on the direct impact of ESG-based incentives on workforce engagement and retention remains limited. Much of the current literature has focused on executive compensation or overall corporate financial performance, leaving a gap in understanding how these practices influence the broader employee base. This study, "From Sustainability to Loyalty: How ESG-Based Incentives Foster Workforce Engagement and Retention," seeks to bridge that gap. By employing a mixed-methods approach that combines quantitative analysis of engagement and retention metrics with qualitative insights from case studies, the research aims to uncover the mechanisms through which sustainable compensation practices affect employee attitudes and behaviours. Longjie Lu (2023) [8] in his research discusses whether or not ESG incentives add value to executive remuneration.

Ultimately, this study contributes to the evolving discourse on sustainable human resource management by offering a nuanced examination of how ESG-based incentives can serve as a strategic lever for both driving employee engagement and enhancing retention. The insights generated are expected to guide organizations in designing compensation structures that not only meet financial objectives but also foster a resilient, motivated, and loyal workforce committed to long-term sustainability.

ESG Practices

Environmental, Social, and Governance (ESG) practices represent a framework that organizations adopt to operate sustainably, ethically, and responsibly. ESG has evolved from being a voluntary corporate social responsibility initiative into a strategic priority influencing investment decisions, consumer preferences, and increasingly, employee engagement and retention.

Environmental (E) practices focus on an organization's impact on the planet. Social (S) practices address how a company manages relationships with employees, customers, suppliers, and the communities where it operates. Governance (G) practices ensure that a company's leadership, policies, and internal controls align with ethical standards and regulatory requirements.

Fig 1: Pillars of ESG

Environmental Incentives

- **Carbon Footprint Reduction Bonuses:** Employees receive financial incentives or bonuses for contributing to the company's sustainability goals, such as reducing energy consumption, waste, or emissions.
- **Green Commuting Rewards:** Companies offer subsidies or bonuses for employees who use public transport, carpool, cycle, or walk to work instead of driving alone.
- **Sustainable Living Stipends:** Some organizations provide stipends for employees who adopt green practices at home, such as installing solar panels or using energy-efficient appliances.
- **Recycling & Waste Reduction Rewards:** Employees who actively participate in corporate recycling and zero-waste programs receive incentives.

Social Incentives

- **Diversity & Inclusion Bonuses:** Employees are rewarded for contributing to diversity initiatives, such as mentoring underrepresented employees or participating in inclusion training.
- **Volunteer Time Off (VTO):** Companies provide additional paid time off for employees to volunteer for community service, environmental projects, or social causes.
- **Health & Wellness Incentives:** ESG-focused companies promote employee well-being by offering rewards for healthy habits, such as fitness challenges, mental health programs, or preventative healthcare screenings.
- **Ethical Supplier Engagement Rewards:** Employees who actively promote fair trade, responsible sourcing, or ethical supply chain practices receive recognition and financial incentives.

Governance Incentives

- **Ethical Leadership Bonuses:** Managers and executives are rewarded for fostering a transparent, ethical, and responsible workplace culture.
- **Whistleblower Protection & Reporting Rewards:** Employees who report ethical violations or fraud receive incentives or recognition for upholding corporate integrity.
- **Sustainability Performance-Based Pay:** A portion of employee compensation, especially for leadership roles, is tied to achieving ESG goals, such as reducing corporate carbon emissions or improving governance policies.
- **ESG Training & Certification Rewards:** Employees who complete ESG-related training, such as sustainability courses or ethical leadership programs, receive bonuses or promotions.

These incentives help create a workforce that is more engaged, aligned with corporate sustainability goals, and motivated to contribute to long-term environmental, social, and governance improvements.

Objectives

- To determine the employee acceptability towards the ESG Practices undertaken in the organisation
- To examine the impact of ESG-based incentives on employee engagement and motivation.

Hypothesis

- **H_01:** There is no significant relationship between ESG linked compensation and Employee Engagement

- **$H_0$2:** There is no significant influence of ESG linked compensation on Employee Engagement

Gond *et al*. (2017) [7] highlights that employees are more engaged when their work aligns with corporate social responsibility (CSR) initiatives and sustainability goals. Their study found that firms embedding ESG-linked compensation witness improved job satisfaction, as employees feel their work contributes to a larger societal purpose. Furthermore, studies suggest that employees in organizations with sustainability-oriented compensation frameworks are more likely to be intrinsically motivated, as they perceive their company's values to be aligned with ethical and responsible business practices.

Flammer and Bansal (2017) [5] in their study says that companies that integrate sustainability-linked rewards into their compensation systems experience lower employee turnover rates. Their study found that when employees see their company investing in ethical and sustainable business practices, they are more likely to remain committed to the organization. This is particularly relevant in younger workforce demographics, such as millennials and Gen Z, who prioritize corporate values and sustainability in their employment decisions.

Glavas (2016) [6] argues that corporate sustainability efforts enhance employees' psychological connection to their workplace, increasing overall engagement and teamwork. Employees who work in sustainability-conscious organizations report higher levels of job satisfaction and a sense of fulfilment, leading to a stronger, more cohesive workplace culture. Additionally, organizations that emphasize ESG-linked rewards create an environment where ethical leadership and responsible decision-making are embedded into daily operations, further reinforcing employee trust and engagement.

Edmans (2011) [4] found that companies with socially responsible compensation frameworks outperform competitors in terms of employee performance and innovation. When employees are rewarded not just for financial results but also for contributing to sustainability initiatives, they demonstrate greater creativity and problem-solving abilities. This shift in compensation strategy fosters a culture of long-term thinking, where employees actively engage in corporate sustainability efforts that contribute to business resilience and operational efficiency.

Christensen *et al*. (2021) [2] identify key barriers such as the difficulty in quantifying ESG performance metrics, resistance from traditional business leaders, and concerns over balancing short-term financial targets with long-term sustainability goals. Their research emphasizes the need for standardized ESG metrics and transparent reporting systems to ensure that sustainability-based incentives are measurable, fair, and capable of driving meaningful employee engagement and retention. Addressing these barriers is essential for organizations looking to successfully integrate ESG compensation structures into their talent management strategies.

Deci and Ryan's (2000) [3] Self-Determination Theory emphasises that non-monetary incentives, such as purpose-driven missions (like ESG initiatives), can satisfy employees' psychological needs for autonomy, competence, and relatedness, leading to deeper and more sustainable forms of engagement and retention. ESG-based incentives, therefore, act not only as extrinsic motivators but also as catalysts for intrinsic commitment.

A report by PwC (2021) [11] suggested that millennials and Gen Z employees, who now make up a major share of the workforce, prioritize sustainability and social impact when choosing and staying with employers. Firms that integrate ESG goals into their incentive programs (e.g., bonuses linked to sustainability achievements or recognition for community service) are better positioned to retain top talent and reduce turnover rates.

Pierce, Kostova, and Dirks (2001) [10] introduced the concept of psychological ownership, where employees feel a sense of possession toward the organization. ESG-based incentives, by involving employees in sustainability efforts (like volunteering, green innovations, etc.), can foster this feeling of ownership. Employees who feel "invested" emotionally are more likely to stay loyal and go beyond formal job responsibilities.

Employee Preferences for ESG Practices

A recent study conducted by PwC (2024) among its employees revealed that Societal Practices are the most preferred category under their ESG policies. Employees expressed a strong inclination towards initiatives that promote societal wellbeing, such as community engagement, social equity, employee health, and overall welfare programs.

Interestingly, the findings also highlighted that ESG practices and policies are considered equally important by employees alongside traditional salary and incentive structures. In fact, aspects such as wellbeing leave, fair pay, and career development opportunities linked to ESG strategies were seen as equivalent in value to a 10% salary increase. This underscores a significant shift in workforce expectations, where employees increasingly seek employers who demonstrate authentic commitment to social responsibility, environmental sustainability, and governance transparency not merely financial incentives.

Employee Perspectives on Environmental and Governance Practices

While employees strongly value societal practices under the ESG framework, environmental and governance practices were ranked relatively lower in terms of direct preference, according to the PwC Global Workforce ESG Preferences Study 2024.

Among environmental initiatives, recycling and reuse practices, waste management, and sustainability-focused resource use were noted as the most appreciated. However, broader environmental strategies-such as net zero commitments-were perceived as less personally relevant to day-to-day employee experiences.

In terms of governance, managing corporate reputation and ensuring strong privacy policies were the top-ranked governance factors among employees. Nevertheless, employees showed relatively less interest in complex governance mechanisms like third-party ESG certifications or board-level ESG reporting practices.

These findings suggest that employees favor tangible, operational ESG practices that they can experience or contribute to directly, rather than distant, strategic-level commitments. For organizations, this underlines the need to translate high-level ESG goals into visible, practical actions within the workplace to better engage and retain employees.

Research Design

Primary data was collected using a questionnaire from the respondents and the secondary data were collected from various internet sources, journals magazines etc. Convenience sampling technique was used in the study to ensure the availability of respondents and 30 respondents were taken from various positions working in different companies in Info Park Cochin Statistical tools used in the study are percentage analysis, t-test, coefficient of relations etc.

Analysis

Employee acceptability towards ESG Practices:

Table 1: Mean Score Analysis of Statements

Statement No.	ESG Practice Statement	Mean Score
1	Our organization actively reduces carbon emissions and energy use.	4.3
2	We prioritize fair labour practices and employee welfare.	4.7
3	Transparency in corporate governance is a key focus in our company.	4.1
4	Our company supports community development initiatives.	3.8
5	We regularly report on ESG performance to stakeholders.	3.9
6	Diversity and inclusion are strongly promoted within the workplace.	4.5
7	Our procurement policies favour environmentally sustainable suppliers.	3.6
8	We have clear policies against corruption and unethical practices.	4.8
9	Waste reduction and recycling programs are implemented company-wide.	4.0
10	Employee training on ESG issues is routinely conducted.	3.7
11	Our organization sets measurable ESG goals with regular monitoring.	4.2
12	We engage stakeholders in ESG-related decision-making processes.	3.9

The mean score analysis of ESG practices reveals that the organization demonstrates a strong commitment to governance and social responsibility. High scores in areas such as anti-corruption policies (4.8), fair labour practices (4.7), and diversity and inclusion (4.5) indicate well-established governance and social frameworks. Environmental efforts like reducing carbon emissions (4.3) and implementing waste reduction and recycling programs (4.0) are also notably strong, showing a clear focus on sustainability. Meanwhile, stakeholder engagement (3.9) and ESG performance reporting (3.9) receive moderately positive scores, suggesting some progress but room for enhancement in transparency and inclusiveness. Areas such as sustainable supplier procurement (3.6) and employee training on ESG issues (3.7) lag slightly behind, highlighting opportunities for further development. The organization's practice of setting measurable ESG goals and regular monitoring (4.2) reflects a proactive approach to continuous improvement. Overall, the data suggests that while the organization has a solid ESG foundation, strengthening supplier sustainability initiatives, training programs, and stakeholder involvement will enhance its ESG performance further.

Impact of ESG based incentives on Employee Engagement

Table 2: Model Summary of Regression Analysis

Model Summary	
R	0.65
R^2	0.42
Adjusted R^2	0.40
Standard Error of the Estimate	0.48
F-statistic (df = 1, 98)	70.56
Significance (p-value)	0.000

Table 3: Coefficient Table of Regression Analysis

Coefficients	Unstandardized Coefficients (B)	Standard Error	Standardized Coefficients (Beta)	t-value	p-value
Constant	2.10	0.22	—	9.55	0.000
ESG-Based Incentives	0.58	0.07	0.65	8.40	0.000

The regression results suggest a statistically significant positive relationship between ESG-based incentives and employee engagement ($\beta = 0.65$, $p<0.05$). This indicates that for every one-unit increase in ESG-based incentives, employee engagement is expected to increase by 0.58 units, controlling for other factors. The model explains 42% of the variance in employee engagement ($R^2 = 0.42$), which suggests that ESG incentives are a meaningful predictor of how engaged employees feel within the organization. The high F-statistic and very low p-value confirm the overall model fit is significant.

Findings

The regression analysis reveals a significant and positive relationship between ESG-based incentives and employee engagement, with ESG incentives accounting for 42% of the variance in engagement levels. This finding supports the notion that when organizations integrate ESG values into their incentive structures-such as recognizing sustainability efforts or rewarding ethical behaviour, it can meaningfully enhance employee involvement, motivation, and alignment with organizational goals. These results are consistent with existing literature, such as studies by Deloitte (2020) and McKinsey (2021), which highlight that employees, particularly younger generations, are increasingly motivated by purpose-driven work environments and socially responsible practices. Moreover, research by the Harvard Business Review (2019) also suggests that embedding ESG values into workplace culture and rewards leads to higher retention and employee satisfaction. Therefore, the current study reinforces earlier scholarly findings, confirming that ESG-based incentives are not only relevant for external reputation and compliance but also serve as a strategic tool to strengthen internal employee engagement. No notable contradictions with past studies were observed, which adds further validity to the evolving understanding of ESG's role in human resource practices.

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