



Green Investment in the Islamic Capital Market: Opportunities and Challenges toward a Green Economy

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ABSTRACT

The escalating challenges of climate change, environmental degradation, and sustainability risks have intensified the demand for financial systems that facilitate the transition toward a green economy. Green investment has emerged as a core pillar of sustainable finance, with capital markets playing a crucial role in mobilizing long-term funding for environmentally responsible activities. Within this context, the Islamic capital market is considered to have strong normative alignment with sustainability principles due to its emphasis on ethics, justice, and accountability. However, existing research integrating green investment, Environmental, Social, and Governance (ESG) frameworks, and Islamic finance remains limited and fragmented. This study aims to systematically examine the opportunities and challenges of green investment within the Islamic capital market in supporting the green economy. Employing a Systematic Literature Review (SLR) approach, this study analyzes peer-reviewed journal articles published between 2015 and 2025. The findings reveal that the Islamic capital market holds significant potential to promote green investment through instruments such as green sukuk, ESG-oriented portfolios, and the integration of ESG with maqasid al-shariah principles. Nevertheless, several challenges persist, including the absence of standardized Sharia-ESG frameworks, divergence in ESG ratings, data quality limitations, and the risk of greenwashing. This study contributes to the literature by offering a comprehensive synthesis and providing policy and research implications to strengthen the role of Islamic capital markets in advancing a sustainable and inclusive green economy.

1. Introduction

Climate change, environmental degradation, and increasing sustainability risks have prompted many countries to shift toward the concept of a green economy, which emphasizes economic growth while simultaneously preserving the environment and promoting social well-being. In this transition, the financial sector plays a crucial role, as it determines the direction of investment and capital allocation. The concept of sustainable finance highlights the importance of incorporating sustainability considerations into investment decisions so

that the financial system can support long-term economic transformation while managing climate-related and other non-financial risks (Edmans & Kacperczyk, 2022). One of the key channels for mobilizing such funding is the capital market, given its ability to raise long-term capital for companies and projects that require sustainable financing.

In practice, many investors rely on the Environmental, Social, and Governance (ESG) framework to assess corporate sustainability risks and opportunities (Asykarulloh et al., 2025). Evidence synthesized from thousands of studies indicates that ESG factors are

associated with firm performance, although the magnitude and direction of this relationship may vary across firms and market conditions (Friede et al., 2015). Investor attention to climate risk has also intensified, as it is increasingly perceived as a material factor affecting firm valuation and portfolio strategies, particularly for long-term oriented institutional investors (Krueger et al., 2020). Moreover, several studies suggest that carbon risk has begun to be priced by the market, implying that environmental issues can have direct implications for asset prices and firms' cost of capital (Bolton & Kacperczyk, 2021).

At the local level, particularly in emerging economies such as Indonesia, the development of sustainable finance and green investment is gaining momentum alongside the rapid growth of the capital market, including the Islamic capital market segment. This growth is supported by an expanding investor base and increasing policy attention toward sustainability. However, the extent to which the Islamic capital market contributes to advancing the green economy remains unclear and underexplored in academic discourse.

Despite the growing interest in ESG-based investing and green finance, several challenges persist in the literature. One major issue is the divergence of ESG ratings across rating agencies, which may confuse investors and reduce the comparability of corporate sustainability performance. Such inconsistencies can weaken the role of ESG information as a reliable signal and complicate the formulation of consistent sustainable investment strategies (Berg et al., 2022). Another challenge is greenwashing, whereby firms make environmental claims that are not aligned with their actual performance, thereby undermining investor trust and the effectiveness of sustainability reporting (Christensen et al., 2021).

Furthermore, prior studies have produced mixed empirical findings regarding the relationship between ESG performance and firm outcomes, suggesting that contextual factors—such as regulatory environments,

investor characteristics, and market maturity—play an important role (Friede et al., 2015; Krueger et al., 2020). Importantly, most existing studies predominantly focus on conventional capital markets, while research integrating green investment, ESG considerations, and Islamic financial principles remains limited, fragmented, and lacks systematic synthesis.

Based on the background and identified gaps, the main research problem can be formulated as follows: the integration of green investment and ESG principles within the Islamic capital market remains insufficiently understood and inconsistently implemented, particularly in terms of aligning Sharia compliance with sustainability criteria, ensuring data comparability, and addressing risks such as greenwashing and ESG rating divergence.

In response to the research problem, this study aims to systematically review the existing literature to: (1) identify the key opportunities for implementing green investment within the Islamic capital market; (2) analyze the major challenges, including ESG rating inconsistencies, data quality issues, and greenwashing risks; and (3) evaluate how ESG and sustainability principles can be integrated with Islamic financial principles to strengthen the role of the Islamic capital market in supporting the green economy.

This study provides both theoretical and practical contributions. Theoretically, it enriches the literature by integrating three important domains—green investment, ESG, and Islamic capital markets—into a comprehensive framework, while also linking sustainability concepts with maqasid al-shariah as a value-based foundation for financial decision-making (Mohd Zain et al., 2024). In doing so, the study addresses fragmentation in prior research and offers a more holistic understanding of sustainable finance within an Islamic context.

Practically, this study offers insights for policymakers, regulators, and practitioners by identifying key barriers and enablers in the

implementation of green investment within the Islamic capital market. The findings can support the development of more consistent ESG standards, enhance transparency in sustainability reporting, and strengthen investor confidence in Sharia-compliant green financial instruments.

The novelty of this study lies in its systematic literature review approach that simultaneously examines green investment, ESG factors, and Islamic capital market principles, particularly within the context of emerging economies. By doing so, it provides a structured and integrative perspective that has been largely absent in prior research, thereby contributing to the advancement of both academic knowledge and policy development in sustainable finance.

2. Literature Review

The literature review establishes the conceptual and theoretical foundation of the study by integrating key theories and synthesizing prior empirical findings related to green investment, the green economy, and the Islamic capital market. This section emphasizes recent scholarly contributions while also incorporating foundational theories that remain conceptually relevant. Furthermore, the review provides a critical basis for identifying research gaps and positioning the current study within the broader academic discourse.

2.1 Conceptual and Theoretical Foundations

2.1.1 Green Investment and Green Economy

a. Green Investment

Green investment refers to the allocation of capital to companies, projects, or financial instruments that explicitly support environmental and sustainability objectives, such as emission reduction, energy efficiency, waste management, and environmentally friendly innovation. Within the green finance literature, green investment is commonly positioned as a key pillar for driving the transformation of economic structures toward

more sustainable production and consumption patterns ([Ozili, 2022](#)). At the corporate level, green investment is closely related to firms' capital allocation decisions for environmental projects, including clean technologies, which are influenced by institutional conditions, policy incentives, and financial constraints ([Rodríguez-Rojas et al., 2022](#)).

From a market perspective, green investment has expanded alongside growing investor demand for sustainable assets. Investors increasingly rely on sustainability-related information when constructing their portfolios, either due to ethical considerations or the perception that sustainability factors are associated with long-term risk and performance ([Amel-Zadeh & Serafeim, 2018](#); [Krueger et al., 2020](#)). Moreover, prior research synthesis indicates a relationship between ESG performance and financial performance, although the magnitude and direction of this relationship vary depending on industry characteristics, country context, and research design ([Friede et al., 2015](#)).

b. Green Economy

The green economy is understood as a development paradigm that emphasizes economic growth while preserving environmental quality and enhancing social welfare. In practice, this paradigm requires a reorientation of economic policies and activities toward more efficient resource use, lower emissions, and reduced negative impacts on ecosystems. To achieve these objectives, the financial system is expected to play an active role as a driver of transition by providing financing that supports sustainable economic activities ([Edmans & Kacperczyk, 2022](#)).

From the perspective of sustainable finance, the green economy is inseparable from long-term risk considerations, particularly climate risk and other non-financial risks that may affect economic stability and firm value. Consequently, the green economy requires a financing ecosystem capable of internalizing environmental and social risks into economic decision-making, including investment and

financing choices ([Edmans & Kacperczyk, 2022](#); [Krueger et al., 2020](#)). In this sense, the green economy is not merely a development goal but also a framework for assessing the resilience of economic systems and firms amid increasing sustainability pressures.

c. ESG as a Framework for Evaluating Green Investment

In contemporary investment practices, ESG is widely used as a framework to assess whether a company or financial instrument can be classified as “sustainable.” ESG enables investors to identify non-financial risks and opportunities that may affect firm value, such as environmental regulatory risk, social reputation risk, and governance-related risk ([Edmans & Kacperczyk, 2022](#)). However, the literature also highlights the existence of significant divergence in ESG ratings across rating agencies, which may lead to what is described as “aggregate confusion” and reduce comparability among firms ([Berg et al., 2022](#)). As a result, the measurement of green investment that relies heavily on a single ESG score may produce inconsistent interpretations.

In addition, the expansion of mandatory sustainability reporting is expected to enhance transparency, yet it also introduces new challenges related to data quality, consistency, and assurance of sustainability information ([Christensen et al., 2021](#)). In the context of green investment, these challenges are closely linked to the risk of greenwashing, where environmental claims are not supported by actual performance. Such practices can ultimately undermine investor confidence and weaken the effectiveness of sustainability policies ([Christensen et al., 2021](#)).

d. Green Investment Instruments within the Financial System

Green investment can be implemented through various financial instruments, including green bonds or sustainability bonds as vehicles for financing sustainable projects, ESG-oriented stocks or portfolios (including

ESG indices), and green finance policies that encourage corporate innovation and ESG performance through regulatory reforms or incentives ([Chen et al., 2022](#); [Ozili, 2022](#)).

The literature suggests that green finance policies can influence corporate behavior, particularly by improving ESG performance and stimulating green innovation ([Chen et al., 2022](#); [Huang et al., 2022](#)). From a market perspective, growing investor attention to carbon risk further indicates that environmental issues are increasingly linked to asset valuation and firms’ cost of capital ([Bolton & Kacperczyk, 2021](#)). Accordingly, green investment operates at the intersection of public policy, investor behavior, and corporate strategy.

e. The Relationship between Green Investment and Green Economy

Conceptually, green investment can be viewed as the “financing engine” of the green economy. The transition toward a green economy requires changes in production and consumption patterns as well as continuous green innovation, all of which depend on long-term financing and credible market signals. Green investment plays a dual role by providing capital and creating incentives for firms to enhance sustainability practices and environmental innovation ([Huang et al., 2022](#); [Ozili, 2022](#)). However, the effectiveness of green investment in advancing the green economy is highly dependent on information quality, governance structures, and policy support. Without these elements, financial markets remain vulnerable to misinformation and greenwashing practices, which may weaken the overall impact of green investment initiatives ([Berg et al., 2022](#); [Christensen et al., 2021](#)).

2.1.2 Islamic Capital Market and Green Investment

a. Islamic Capital Market: Concept and Characteristics

The Islamic capital market constitutes a segment of the capital market that operates

based on Sharia principles, particularly the prohibition of *riba* (interest), *gharar* (uncertainty), and *maysir* (speculation), as well as restrictions on business activities that are not compliant with Sharia regulations. In practice, Sharia compliance within the capital market is implemented through a screening process that evaluates the nature of business activities and specific financial ratios. As a result, instruments classified as Sharia-compliant are considered to meet ethical standards and prudential requirements.

This ethical orientation leads the Islamic capital market to be frequently viewed as having value alignment with the sustainable development agenda. By emphasizing justice, transparency, and accountability in economic activities, the Islamic capital market provides a normative foundation that is consistent with the principles of sustainability and responsible investment ([Mohd Zain et al., 2024](#)).

b. Green Investment from the Perspective of the Islamic Capital Market

Green investment in the context of the Islamic capital market refers to the allocation of capital to Sharia-compliant instruments—such as Islamic stocks, *sukuk*, and Islamic mutual funds—that support environmental and social sustainability objectives. Within the green economy framework, green investment is positioned as an important mechanism for directing capital toward low-emission activities, energy efficiency, sustainable resource management, and environmentally friendly innovation ([Ozili, 2022](#)).

At the firm level, green investment is also associated with corporate decisions to undertake green capital expenditure and environmental innovation, which are influenced by policy incentives and institutional conditions ([Rodríguez-Rojas et al., 2022](#)). Given that the Islamic capital market normatively emphasizes *maslahah* (public benefit), green investment within this market can be viewed as an investment approach that integrates financial objectives with sustainability goals within a unified ethical

framework ([Mohd Zain et al., 2024](#); [Sulistiyo et al., 2025](#)).

c. ESG and Maqasid al-Shariah as a Sustainability Evaluation Framework

ESG is widely used as a framework for assessing corporate sustainability risks and opportunities. In capital market practices, ESG assists investors in identifying non-financial risks that may affect firm value, including environmental risk, social risk, and governance-related risk ([Edmans & Kacperczyk, 2022](#)). However, the literature also highlights a significant challenge in the form of divergence in ESG ratings across rating agencies, which leads to inconsistent ESG scores and may create uncertainty in investment decision-making ([Berg et al., 2022](#)).

Within the context of Islamic finance, efforts to integrate ESG with *maqasid al-shariah* aim to develop an evaluation framework that goes beyond procedural compliance and focuses on actual outcomes related to social and environmental well-being (*maslahah*). Such integration is essential to strengthen the legitimacy of green investment in Islamic capital markets and to reduce the risk of inaccurate or overstated sustainability claims ([Mohd Zain et al., 2024](#)).

d. Islamic Green Investment Instruments and Market Mechanisms

One of the financial instruments most commonly associated with green investment in Islamic finance is green *sukuk*, namely *sukuk* whose issuance proceeds are allocated specifically to environmentally friendly projects. More broadly, the development of green finance instruments—including green bonds and other sustainability-oriented instruments—is considered effective in expanding financing for green projects and encouraging corporate behavioral change toward more sustainable practices ([Ozili, 2022](#)).

From a policy perspective, green finance reforms and regulatory support can influence firms to improve ESG performance and engage

in green innovation ([Chen et al., 2022](#)). In the context of the Islamic capital market, the presence of a clear regulatory framework and high-quality sustainability information is crucial to ensure that Sharia-compliant green instruments gain investor trust and develop in a stable and sustainable manner.

e. Implementation Challenges: Data Quality, Greenwashing, and Comparability

Despite its considerable potential, green investment in the Islamic capital market faces several challenges related to the quality and comparability of sustainability information. Differences in ESG ratings across institutions indicate that sustainability measurement has not yet been fully standardized, making it difficult for investors to compare firms' sustainability performance accurately ([Berg et al., 2022](#)).

In addition, the risk of greenwashing represents a critical issue, as environmental claims that are not supported by actual performance can undermine investor confidence and weaken the effectiveness of sustainability reporting ([Christensen et al., 2021](#)). These challenges are particularly relevant for Islamic capital markets, where the legitimacy of Sharia-compliant instruments is derived not only from formal compliance but also from public trust in their integrity and real impact. Therefore, strengthening reporting governance, enhancing assurance mechanisms, and achieving clearer integration between Sharia principles and sustainability indicators are increasingly urgent needs.

2.2 Review of Empirical Studies

Empirical studies on green investment and sustainability indicate a growing integration between financial performance and ESG considerations ([Sitohang & Utomo, 2026](#)). Prior research synthesis suggests that ESG performance is associated with financial performance; however, the relationship varies depending on industry characteristics, country context, and methodological approaches

([Friede et al., 2015](#)). More recent studies emphasize that green finance policies can significantly influence corporate behavior by improving ESG performance and stimulating green innovation ([Chen et al., 2022](#); [Huang et al., 2022](#)).

In capital markets, investor behavior increasingly reflects sensitivity to sustainability-related risks, particularly carbon risk, which has been shown to affect asset valuation and firms' cost of capital ([Bolton & Kacperczyk, 2021](#)). This indicates that sustainability is no longer a peripheral consideration but a core determinant of financial decision-making.

However, empirical evidence also highlights several limitations. One major issue is the inconsistency of ESG ratings across different agencies, which creates measurement uncertainty and complicates cross-study comparisons ([Berg et al., 2022](#)). Additionally, while sustainability reporting has expanded significantly, concerns remain regarding data reliability, comparability, and assurance, which may weaken the credibility of reported ESG performance ([Christensen et al., 2021](#)).

In the context of the Islamic capital market, empirical studies remain relatively limited. Existing research suggests that Sharia-compliant investments are aligned with sustainability principles, particularly through ethical screening and the emphasis on social welfare ([Mohd Zain et al., 2024](#)). Nevertheless, there is still insufficient empirical evidence examining how green investment operates within Islamic financial systems, particularly in relation to ESG integration and real environmental impact.

2.3 Identification of the Research Gap

Based on the synthesis of theoretical and empirical literature, several research gaps can be identified. First, although green investment is widely recognized as a driver of the green economy, its effectiveness is highly dependent on the quality and consistency of sustainability information. The persistence of ESG rating divergence and greenwashing risks indicates

that existing measurement frameworks are still inadequate ([Berg et al., 2022](#); [Christensen et al., 2021](#)).

Second, while extensive studies have examined green investment in conventional financial markets, limited attention has been given to its application within the Islamic capital market. In particular, the integration between ESG frameworks and *maqasid al-shariah* remains underexplored, both conceptually and empirically ([Mohd Zain et al., 2024](#)).

Third, prior studies tend to focus on developed markets, leaving a contextual gap in emerging markets where institutional frameworks, regulatory environments, and market maturity differ significantly. This limitation restricts the generalizability of existing findings and highlights the need for context-specific analysis.

Therefore, this study addresses these gaps by examining green investment within the Islamic capital market framework, with particular attention to sustainability measurement challenges, ethical integration, and contextual relevance.

2.4 Development of the Conceptual Framework

This study focuses on the interrelationship between green investment, sustainability frameworks (ESG), and the broader objective of achieving a green economy within the context of the Islamic capital market. Green investment serves as the primary mechanism for allocating financial resources toward environmentally sustainable activities, while ESG functions as an evaluative framework for assessing sustainability performance and risks ([Edmans & Kacperczyk, 2022](#)).

Within the Islamic capital market, the integration of ESG with *maqasid al-shariah* strengthens the ethical and sustainability dimensions of investment decisions, aligning financial objectives with social and environmental welfare ([Mohd Zain et al., 2024](#)). At the same time, factors such as data

quality, reporting standards, and governance mechanisms influence the effectiveness of green investment in achieving sustainability outcomes.

2.5 Hypotheses or Research Propositions

This study does not formulate specific hypotheses, as it adopts a conceptual and theoretical approach rather than a quantitative empirical design. Instead, the study aims to provide a comprehensive analytical understanding of green investment within the Islamic capital market and its role in supporting the green economy, while addressing existing theoretical and empirical gaps identified in the literature.

3. Research Methods

This study adopts a qualitative approach using a Systematic Literature Review (SLR) method to examine the development of green investment in the Islamic capital market and its relevance to the green economy agenda. The methodology is designed to ensure transparency, rigor, and replicability by systematically identifying, evaluating, and synthesizing relevant academic literature. The alignment between the research design, data collection, and analytical techniques enables a comprehensive understanding of research trends, key themes, and challenges within the field.

3.1 Research Design

This study employs a qualitative research design through a Systematic Literature Review (SLR). The SLR approach is selected due to its ability to provide a structured and transparent synthesis of existing academic studies, allowing for the identification of research trends, conceptual developments, and gaps in the literature. This design is particularly suitable for addressing the research objectives, which focus on understanding the role and evolution of green investment within the Islamic capital market in supporting the green economy agenda.

3.2 Research Context and Setting

The research is situated within the context of Islamic finance and capital markets, with a specific focus on green investment and sustainability practices. The study encompasses both global and national perspectives, particularly emphasizing literature related to Islamic capital markets. The chosen context is relevant due to the increasing global attention toward sustainable finance and the growing role of Islamic financial instruments, such as green sukuk, in supporting environmentally responsible economic development.

3.3 Population and Sample / Research Participants

The population of this study consists of academic publications related to green investment, ESG, sustainability, and Islamic capital markets. The sample includes peer-reviewed journal articles published between 2015 and 2025. The selection process follows specific inclusion criteria: (1) articles published in peer-reviewed journals; (2) studies discussing green investment, ESG, sustainability, or Islamic capital markets; (3) articles written in English or Indonesian; and (4) conceptual, empirical, or review-based studies. Exclusion criteria include: (1) non-academic publications such as opinion pieces, reports, or editorials; (2) studies not directly related to capital markets or Islamic finance; and (3) duplicate articles. This selection ensures the relevance, quality, and credibility of the data analyzed.

3.4 Data Sources and Data Collection

This study utilizes secondary data obtained from academic literature. Data collection was conducted through systematic searches in several databases, including Google Scholar, Garuda, and selected international journal databases. These databases were chosen to capture both global and national research perspectives. The search process employed specific keywords, such as green investment, green finance, Islamic capital

market, sharia capital market, ESG, sustainable finance, green sukuk, and Islamic finance and sustainability. Boolean operators (“AND” and “OR”) were used to refine the search results. The literature selection process involved three stages: (1) identification of articles through keyword searches; (2) screening of titles and abstracts; and (3) full-text review to ensure alignment with the research objectives.

3.4 Measurement of Variables and Research Instruments

As a qualitative SLR study, this research does not employ quantitative measurement instruments. Instead, key concepts such as green investment, ESG implementation, sustainability, and Islamic capital market characteristics are operationalized through thematic categorization based on existing literature. The indicators used are derived from prior studies published in reputable journals, ensuring conceptual validity and consistency with existing research frameworks.

3.6 Data Analysis Techniques

The selected articles were analyzed using thematic analysis. This technique involves systematically categorizing the literature into key themes, including: (1) the role of green investment in supporting the green economy; (2) the application of ESG frameworks in capital markets; (3) the characteristics and potential of Islamic capital markets for sustainable finance; and (4) challenges such as ESG rating divergence and greenwashing. Through this process, patterns, similarities, and differences across studies were identified and interpreted to generate meaningful insights.

3.7 Validity, Reliability, and Trustworthiness

To ensure the trustworthiness of the study, several strategies were applied. Credibility was enhanced through the use of transparent inclusion and exclusion criteria and a systematic selection process.

Dependability was ensured by clearly documenting each stage of the literature review process. Confirmability was supported by cross-referencing multiple studies and databases to reduce selection bias. These procedures strengthen the rigor and reliability of the findings.

3.8 Ethical Considerations

This study adheres to ethical research standards by utilizing publicly accessible academic sources and properly acknowledging all referenced works. No primary data involving human participants were collected; therefore, issues such as informed consent and confidentiality are not applicable. However, academic integrity is maintained through accurate citation and avoidance of plagiarism.

3.9 Research Procedure

The research procedure was conducted in several structured stages: (1) defining the research objectives and questions; (2) developing search keywords and strategies; (3) identifying relevant literature from selected databases; (4) screening titles and abstracts; (5) conducting full-text reviews based on inclusion and exclusion criteria; (6) categorizing selected articles into thematic groups; and (7) analyzing and synthesizing the findings to draw conclusions.

3.10 Methodological Limitations

This study has several limitations. First, the reliance on selected databases may result in the exclusion of relevant studies not indexed within those sources. Second, the use of specific keywords may limit the scope of retrieved articles. Third, as a qualitative SLR, the findings are interpretative and may be subject to researcher bias. Despite these limitations, efforts have been made to ensure transparency and rigor throughout the research process.

4. Results and Discussion

This section reports and discusses the empirical findings of the study in a structured

and transparent manner. The Results subsection focuses on presenting the outcomes of data analysis objectively, while the Discussion subsection provides a critical interpretation of the findings, linking them to relevant theories and prior studies.

4.1 Research Results

4.1.1 Sample Description and Descriptive Statistics

This study employs a qualitative approach using a Systematic Literature Review (SLR). The sample consists of selected academic articles related to green investment, ESG frameworks, and Islamic capital markets. The reviewed literature reflects a diverse range of contexts, including global and emerging markets, with particular attention to sustainable finance practices and Islamic financial systems. The descriptive overview indicates a growing number of publications focusing on the intersection between sustainability and Islamic finance.

4.1.2 Data Quality and Preliminary Analysis

The selected studies were systematically evaluated based on relevance, publication quality, and methodological rigor. Inclusion criteria ensured that the articles were sourced from reputable journals and aligned with the research objectives. The screening process resulted in a refined dataset suitable for thematic analysis.

4.1.3 Main Analytical Results

The analysis identifies four major themes emerging from the literature:

a. Green Investment and Sustainable Finance Trends

The reviewed literature indicates a growing global emphasis on green investment as a core component of sustainable finance. Green investment is widely recognized as an effective mechanism for directing capital toward environmentally responsible activities, including renewable energy, energy efficiency, and sustainable infrastructure. Several studies highlight that green investment is increasingly

viewed not only as an ethical choice but also as a strategic response to long-term environmental and climate-related risks ([Edmans & Kacperczyk, 2022](#); [Ozili, 2022](#)).

Within capital markets, the rise of green bonds, sustainability-linked instruments, and ESG-oriented portfolios reflects a structural shift in investor preferences. Investors increasingly consider sustainability-related information when allocating capital, particularly in response to climate risk and regulatory pressure. Empirical evidence suggests that firms engaging in green investment or demonstrating strong ESG performance tend to gain improved access to capital markets, although financial outcomes may vary depending on market conditions and institutional settings ([Friede et al., 2015](#); [Bolton & Kacperczyk, 2021](#); [Sagita & Pebriyani, 2025](#)). These findings underscore the importance of green investment as both a financing tool and a market signal within the broader green economy framework.

b. ESG Frameworks in Capital Market Practices

The ESG framework emerges as a dominant tool for evaluating sustainability performance in capital markets. Many studies emphasize that ESG information helps investors assess non-financial risks that are increasingly material to firm value, such as environmental liabilities, social controversies, and governance weaknesses ([Amel-Zadeh & Serafeim, 2018](#); [Krueger et al., 2020](#)). As a result, ESG has become a common reference point for identifying green investment opportunities.

However, the literature also points to significant limitations of ESG-based assessments. One of the most frequently cited issues is the divergence of ESG ratings across different rating agencies. Differences in methodology, weighting schemes, and data sources lead to inconsistent ESG scores for the same firm, reducing comparability and potentially confusing investors ([Berg et al., 2022](#)). This inconsistency weakens the

effectiveness of ESG as a universal benchmark for green investment and raises concerns about its reliability as a decision-making tool.

In addition, the expansion of mandatory sustainability reporting is seen as a double-edged sword. While enhanced disclosure can improve transparency, it may also increase compliance complexity and create opportunities for symbolic rather than substantive sustainability practices if not accompanied by robust verification mechanisms ([Christensen et al., 2021](#)).

c. Opportunities for Green Investment in Islamic Capital Markets

The literature highlights that Islamic capital markets possess distinctive characteristics that align well with the principles of green investment. Sharia principles emphasize ethical conduct, risk sharing, transparency, and the avoidance of speculative and harmful activities, which are conceptually consistent with the objectives of the green economy. As a result, Islamic capital markets are increasingly viewed as a potential platform for advancing sustainable and responsible investment ([Mohd Zain et al., 2024](#)).

Several studies identify green sukuk as a promising instrument that bridges Islamic finance and green investment. By allocating proceeds to environmentally beneficial projects, green sukuk offers a Sharia-compliant mechanism for financing sustainable development initiatives. Moreover, the integration of ESG considerations with maqasid al-shariah is seen as an opportunity to strengthen the normative foundation of sustainability assessment in Islamic finance, moving beyond procedural compliance toward outcome-oriented evaluation ([Mohd Zain et al., 2024](#)).

In emerging markets, including Indonesia, the growing size of Islamic capital markets and increasing policy attention to sustainable finance further enhance the potential role of green investment within Sharia-based financial systems. This creates

opportunities for Islamic capital markets to contribute more actively to national and global green economy agendas.

d. Challenges and Constraints in Implementation

Despite these opportunities, the literature consistently identifies several challenges that hinder the effective implementation of green investment in Islamic capital markets. A key issue is the lack of an integrated and standardized framework that combines Sharia compliance with ESG criteria. Without clear and unified standards, the classification and evaluation of “green” Islamic financial instruments remain fragmented across institutions and jurisdictions.

Another major concern is greenwashing, which poses risks to investor trust and market credibility. Studies emphasize that weak assurance mechanisms and inconsistent sustainability reporting increase the likelihood of overstated environmental claims, undermining the legitimacy of green investment initiatives ([Christensen et al., 2021](#)). This challenge is particularly critical for Islamic capital markets, where ethical credibility is a central pillar of legitimacy.

Furthermore, mixed empirical findings on the relationship between ESG performance and financial outcomes suggest that green investment does not automatically translate into superior financial performance. Contextual factors such as regulatory quality, investor literacy, and market maturity play an important role, especially in developing countries ([Friede et al., 2015](#); [Krueger et al., 2020](#)). These findings highlight the need for more context-specific research and policy design tailored to Islamic capital markets.

4.1.4 Hypothesis Testing Results / Key Findings

The study reveals key findings structured around the research objectives:

- a. Green investment is increasingly integrated into global financial systems as part of sustainable finance.

- b. ESG frameworks play a central but imperfect role in guiding investment decisions.
- c. Islamic capital markets offer significant opportunities for green investment through instruments such as green sukuk.
- d. Implementation challenges persist, particularly in standardization, credibility, and contextual effectiveness.

4.2 Research Discussion

4.2.1 Interpretation of Key Findings

The findings indicate that green investment has evolved into a strategic component of modern financial systems, particularly in response to climate-related risks. Within Islamic capital markets, the alignment between Sharia principles and sustainability objectives strengthens the relevance of green investment as a viable financing mechanism.

4.2.2 Comparison with Previous Studies

The results are consistent with prior studies emphasizing the growing importance of ESG in investment decisions ([Amel-Zadeh & Serafeim, 2018](#); [Krueger et al., 2020](#)). However, this study also reinforces concerns raised by [Berg et al. \(2022\)](#) regarding ESG rating inconsistencies and by [Christensen et al. \(2021\)](#) regarding potential greenwashing practices. In line with [Friede et al. \(2015\)](#), the relationship between ESG performance and financial outcomes remains inconclusive.

4.2.3 Theoretical Contributions

This study contributes to the literature by integrating sustainable finance theory with Islamic finance principles. It extends existing frameworks by highlighting the compatibility between ESG and maqasid al-shariah, thereby offering a more holistic approach to evaluating sustainability in Islamic capital markets.

4.2.4 Practical and Policy Implications

The findings suggest that regulators and policymakers should develop standardized frameworks that integrate ESG and Sharia

principles to enhance consistency and credibility. Financial institutions are encouraged to adopt robust verification mechanisms to mitigate greenwashing risks. Additionally, increasing investor awareness and literacy is essential to support the effective implementation of green investment strategies.

4.2.5 Integration with the Research Gap

This study addresses the research gap by providing a structured synthesis of how green investment operates within Islamic capital markets, an area that remains underexplored. It bridges the gap between conventional ESG frameworks and Islamic finance principles, offering new insights into their integration.

4.2.6 Acknowledgement of Study Limitations

This study is limited by its reliance on secondary data from existing literature, which may not fully capture real-time developments in green investment practices. Additionally, variations in regional contexts and methodological approaches across studies may affect the generalizability of the findings.

5. Conclusion

This study synthesizes the main findings from a systematic literature review on green investment in the Islamic capital market and its relevance to the green economy agenda. The results demonstrate that green investment is increasingly recognized as a key component of sustainable finance, particularly in channeling capital toward environmentally responsible and socially beneficial activities. The findings also reveal that Islamic capital markets possess strong normative foundations aligned with sustainability principles, although their implementation remains constrained by several structural and practical challenges. Overall, this study confirms that while the Islamic capital market holds significant potential to support the green economy, its effectiveness depends on improvements in regulatory frameworks, data quality, and market practices.

5.1 Summary of Key Findings

The study finds that green investment has gained growing importance within capital markets, driven by increasing awareness of environmental and non-financial risks. ESG frameworks are widely used to evaluate sustainability performance, although inconsistencies in measurement and reporting persist. The Islamic capital market is conceptually aligned with green economy principles through Sharia values such as justice, transparency, and accountability. Instruments such as green sukuk and ESG-oriented Sharia-compliant portfolios highlight its potential contribution to sustainable development. However, the implementation of green investment remains limited due to challenges including the lack of integrated Sharia-ESG standards, inconsistent ESG ratings, limited sustainability data, and the risk of greenwashing. In addition, empirical evidence on the financial impact of ESG performance remains inconclusive, particularly in developing countries.

5.2 Theoretical Contributions

This study contributes to the literature by bridging the conceptual intersection between Islamic finance principles and green investment frameworks. It extends existing theoretical discussions by demonstrating that Sharia principles are not only ethically compatible with sustainability but can also serve as a foundational framework for advancing green finance. Furthermore, the study highlights the gap in integrating ESG criteria with maqasid al-shariah, offering a novel perspective for future theoretical development. By synthesizing prior studies, this research refines the understanding of how Islamic capital markets can be positioned within the broader discourse of sustainable finance and green economy transitions.

5.3 Practical and Policy Implications

The findings suggest several important implications for regulators, practitioners, and policymakers. Regulators are encouraged to

develop integrated frameworks that combine Sharia compliance with ESG standards to improve consistency and credibility in green investment classification. Market participants should enhance sustainability disclosure practices and adopt stronger assurance mechanisms to mitigate greenwashing risks. Improving the quality and comparability of ESG data is essential for informed investment decisions. Additionally, increasing investor literacy regarding green investment and Islamic sustainability concepts can strengthen market discipline and support the growth of credible green financial products.

5.4 Limitations of the Study

This study is limited by its reliance on secondary data through a systematic literature review, which may be influenced by publication bias and variations in research quality across studies. The findings are also constrained by the scope of the reviewed literature, particularly the limited availability of empirical studies in developing country contexts. As a result, the generalizability of the conclusions may be restricted, especially in capturing real-world implementation dynamics across different Islamic capital markets.

5.5 Directions for Future Research

Future research is encouraged to conduct empirical and comparative studies examining the performance of green investment in Islamic capital markets across different countries and institutional settings. Further investigation into the integration of ESG frameworks with maqasid al-shariah is needed to develop more comprehensive and operational models. Additionally, future studies may explore alternative methodologies, incorporate broader datasets, and examine additional variables such as regulatory quality, institutional support, and investor behavior to provide deeper insights into the effectiveness of Islamic green finance in supporting the green economy.

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