



The effect of environmental, social, and governance disclosure on company value and profitability

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Abstract

This study aims to test hypotheses and produce empirical findings related to the influence of environmental, social, and governance disclosure on company value and profitability. This study uses a purposive sampling technique. The data used in this study are the financial statements of non-financial companies listed on the IDX during the 2019-2022 period as many as 35 companies with a sample of 95. Hypothesis testing in this study uses multiple linear regression analysis with the help of the SPSS version 26 program.

The independent variables used were environmental, social, and governance disclosures which were proxied using the ESG disclosure score. In addition, the dependent variables are the value of the company that is proxied using Tobin's Q and the profitability that is proxied using Return on Asset (ROA).

The results of the research conducted show that the ESG disclosure score has a positive and significant effect on company value and profitability.

Keywords: Environmental, social, and governance disclosure, company value, and profitability

Introduction

The increasing competition in the business world in Indonesia encourages companies to develop and implement strategic plans that can improve their competitiveness in the long run. To assess the effectiveness of these strategies, financial performance is one of the most important aspects that must be considered. Financial performance serves as a benchmark for understanding how well a company is operating today and predicting potential future growth. For managers, maintaining high financial performance is a top priority, as it plays a key role in shaping the structure and development of the company. Strong financial performance provides stakeholders with confidence in the company's stability and potential for future success. In this study, financial performance is seen using company value and profitability (Le Thi Kim *et al.*, 2021) ^[8]. The value of a company has an important position today because it can affect the financial performance of a company and increase investor confidence. In addition, the company's value is also a benchmark for the company's operational ability which is quantified into a value. High-value companies are likely to gain public trust. Capital markets provide companies with the opportunity to maximize their value by providing comprehensive information disclosure, such as publishing reports detailing the company's operational performance. A good company's performance shows a high valuation of the company because it is usually followed by an increase in the stock, which will ultimately result in an increase in its value. The rising share price of a company reflects its greater value (Christy & Sofie, 2023).

In addition to considering the value of the company, investors also attach great importance to the financial health of the company. Financial health is essential to understanding the stability and growth potential of a company. Profitability is one of the main indicators of financial health that assesses how capable a company is in earning profits through its operational activities by optimizing the use of assets.

Profitability is also very important because it is able to show the extent to which the company maintains and develops its financial wealth over time. Any company wants great profitability because it demonstrates strong financial performance as well as the ability to fund future growth and development (Salim & Franciska, 2020) ^[12].

Along with the paradigm shift towards sustainable practices, investors are now making corporate value and profitability a critical component of their decisions. In addition, the growing global interest and awareness related to non-financial factors puts pressure on companies to step up their sustainability efforts. One of the key components that affect the determination of company value and profitability is environmental, social, and governance disclosure. Investors, suppliers, employees, customers, and governments today want more from companies to consider non-financial factors and report their performance through sustainability reports called ESG reports by categorizing their performance on three components, namely environmental, social, and governance. This report is a communication tool that plays an important role in convincing investors of the company's attitude. This is also supported by increasing demand from investors and other stakeholders regarding the disclosure of additional information about sustainability and business plans (Kartika *et al.*, 2023) ^[7].

Research and statistics conducted by the OJK show that only 8 percent or as many as 54 companies out of 688 published sustainability reports for the 2019 period and increased in 2021 to 19 percent or as many as 135 companies out of 709 listed on the Indonesia Stock Exchange. In addition, based on Bloomberg data, a total of 79 out of 776 nonfinancial companies listed on the Indonesia Stock Exchange reported ESG disclosure score during the 2019-2022 period. This indicates a low level of awareness regarding the disclosure of ESG reports in Indonesia. The implementation of ESG has not been widely carried out in all Indonesia companies because many companies still have difficulty applying sustainability

principles and have not disclosed relevant information to the public. International Association for Public Participation Indonesia has identified various challenges that hinder the effective implementation of ESG, including limited corporate understanding of ESG, inadequate resources, and high consulting costs related to the management of ESG aspects (Fajri Yudha & Rahman, 2024) [3].

Literature Review

According to the stakeholder theory, it needs to be emphasized if the company must be responsible to several related parties. This includes internal stakeholders, which contain shareholders, employees, and customers. In addition, it also includes external stakeholders, which include suppliers, creditors, and the government. According to this theory, companies have control over important resources so companies need to maintain positive relationships with stakeholders in order to achieve superior performance compared to their competitors. This theory also explains that the company does not solely prioritize personal interests, but must also help all parties involved, including stakeholders. Therefore, support from stakeholders will affect the company's survival. By transparently disclosing information about the company's operations, which includes both financial and nonfinancial aspects, the company will gain support from stakeholders (Malik & Kashiramka, 2024) [9]. The company's commitment to implementing sustainable practices can strengthen its relationships with stakeholders and attract new capital. One important aspect of this commitment is the disclosure of non-financial information, namely ESG

(environmental, social, and governance). Companies that seek to meet the needs and improve the welfare of their stakeholders are considered to be able to operate well and can create a positive reputation in public judgment. A positive image will increase trust and loyalty, which directly contributes to an increase in the company's value. In addition, it will also have the potential to increase sales and return on assets (ROA) overall. By increasing transparency and disclosing their sustainable practices through ESG disclosure, the company is able to foster trust with stakeholders to generate profits in the long term (Risal *et al.*, 2024) [11].

The Effect of Environmental, Social, and Governance Disclosure on Company Value Stakeholders, including investors, customers, employees, and regulators, are increasingly concerned about how companies manage their environmental impacts, be accountable to the community, and implement governance practices. When it shows high performance in these aspects, it will convince stakeholders that the company has met their expectations which can ultimately increase the support and loyalty of stakeholders. This means that there is alignment with the stakeholder theory, because it affirms the company's responsibility to the various parties involved. By implementing ESG effectively, it can increase investor confidence and get more attention, thereby improving their reputation. As a result, the value of a company that has increased will be considered a sustainable and ethical entity (Prabawati & Rahmawati, 2022) [10]. Results of previous research that has been researched

Aydoğmuş *et al.* (2022) and also Jeanice & Kim (2023) [6] reinforcing the formulation of a hypothesis by showing that ESG can increase the value of the company. Thus, if the company upholds environmental, social, and governance practices, it will be able to significantly strengthen relationships with its stakeholders. In addition, stakeholders can also see the company's commitment to sustainability through transparent ESG reporting. This transparency which in turn will produce a positive effect on the company's value through an increase in the share price, thus attracting stakeholders to invest and support the company as it is in line with their values and expectations. Based on the explanation and results of previous research, the researcher developed the following hypothesis:

H₁: Environmental, Social, and Governance Disclosure has a positive effect on the Company's Value.

The Effect of Environmental, Social, and Governance Disclosure on Profitability

Disclosure of information about ESG performance allows companies to optimize credibility and foster trust among stakeholders. This belief is essential for sustainability and long-term success, as has been explained in the stakeholder theory. Companies that are open about ESG practices are seen as preferred by the public, so they can increase their loyalty. This can improve a company's reputation, potentially leading to increased sales and overall return on assets (ROA). According to Risal *et al.* (2024) [11], strong ESG disclosure practices not only increase the value of a company, but can also provide tangible financial benefits. Improving a company's reputation through ESG performance efforts can result in increased sales because consumers are more likely to buy from companies that they consider ethical and socially responsible, which will have an impact on increasing the company's ROA.

Companies that prioritize ESG factors tend to have an improvement in their profitability as well as financial performance, as ESG practices can result in cost savings, improved risk management, and improved reputation, all of which contribute to increased profitability. Therefore, adopting and implementing ESG disclosure practices effectively is essential for companies seeking to achieve long-term profitability. This also shows alignment with the findings of the research carried out Aydoğmuş *et al.* (2022) [1] and Ghazali & Zulmaita (2020) [4] which shows that ESG can increase profitability. Based on the explanation and results of previous research, the researcher developed the following hypothesis:

H₂: Environmental, Social, and Governance Disclosure has a positive effect on Profitability.

Method

Table 1: Dependent and Independent Variable Measurements

Variable	Measurement
Company Values	(Equity Market Value + Debt Market Value) / (Equity Book Value + Debt Book Value)
Profitability	Net Profit / Total Assets
Environmental, Social, and Governance Disclosure	Bloomberg-based ESG Disclosure Score

Refers to Sugiyono (2019) ^[13], population is defined as to reach a conclusion. In this study, the population in an area that includes objects or subjects with certain question is non-financial companies registered on the traits and qualities that the researcher has determined IDX in the 2019-2022 period.

The purpose of this study is to determine the influence of environmental, social, and governance disclosure on company value and profitability. This study utilizes secondary data that is quantitative in the form of annual reports of non-financial companies and is recorded on the official websites of the Indonesia Stock Exchange and Bloomberg. The methods used include documentation techniques such as journals, news articles, theses, the internet, and other literature. This research involves two dependent variables, namely company value and profitability and one independent variable, namely environmental, social, and governance disclosure. The value of a company is measured through Tobin's Q which can indicate whether a company's shares are classified as cheap (undervalued) or expensive (overvalued). Profitability can be measured using Return on Asset, which can assess how effective management is in achieving profits from owned assets. ESG disclosures are measured in the form of scores, with Bloomberg databases. Bloomberg's ESG Disclosure Score represents the percentage of things a company discloses based on Bloomberg's standard disclosure criteria. Meanwhile, the sample used focuses on entities that have an ESG disclosure score. The sample selection method used is purposive sampling, where this sample determination method uses special characteristics or conditions that have been determined.

Table 2: Sample Selection

It	Information	Sum
1	Non-financial companies listed on the Indonesia Stock Exchange during the period 2019-2022	776
2	Non-financial companies that do not have an ESG Disclosure Score	(697)
3	Non-financial companies that have no profit on their financial statements and have suffered losses since 2019-2022	(26)
4	Non-financial companies that did not provide complete information regarding the variables used by the researcher during the 2019-2022 period	(9)
Total non-financial companies that can be used as research objects		44
Total samples		176
Outlier on a sample of research data		(81)
The number of final samples used and meeting the research criteria		95

Result

Descriptive Statistical Analysis

From the descriptive statistical test produced in Table 2, it is shown that the number of non-financial company data samples selected (N) is 95 research samples. The variable of company value measured through Tobin's Q shows a minimum value of 0,58 and a maximum value of 1,95. PT Media Nusantara Citra Tbk in 2022 has the lowest Tobin's Q ratio or less than 1, meaning that the company is classified as cheap (undervalued) because its book value is higher than its market value. Meanwhile, PT Tower Bersama Infrastructure Tbk in the same year had the highest Tobin's Q ratio or more than 1, meaning that the company is

classified as overvalued and shows good growth prospects, because the market value of the company's assets is higher compared to the book value of the company's assets. On the other hand, the mean value of this variable is 1,1667. Then, the result of the standard deviation value of Tobin's Q of 0,33697 was obtained, which means that the company value variable in this test has an even or homogeneous distribution of data, because the value of the mean as a whole obtains the largest value than the standard deviation value.

The profitability variable, which is measured by Return on Asset (ROA) by dividing net income by total assets, shows a minimum value of 0,02 and a maximum value of 13,37. PT Barito Pacific Tbk in 2022 has the lowest ROA value or less than 1, meaning that not all assets in the company can generate profits, so the rate of return in 2022 is relatively low. Meanwhile, PT Adaro Energy Indonesia Tbk in 2021 has the highest ROA value or more than 1, meaning that every asset in the company can generate profits, so the rate of return in 2021 is relatively high. In addition, the mean value of ROA is 4,7992 which indicates that the average of each asset owned by the company produces a profit or profit of 4,7992. Furthermore, the resulting standard deviation value is 3,26506 which means that the profitability variable in this study has an even distribution of data due to the value of the mean the overall ROA has the largest value compared to the standard deviation value.

The environmental, social, and governance disclosure variables measured through the ESG disclosure score showed a minimum value of 24,62 and a maximum value of 69,12. PT Erajaya Swasembada Tbk in 2019 has the lowest ESG disclosure score, while PT Vale Indonesia Tbk in 2022 is the owner of the maximum value. This shows that the two companies do not have a maximum ESG disclosure score, because each company's score is still below 100. In addition, the average value of the ESG *Disclosure Score* is 42,6854 which means that the company that disclosed the average ESG disclosure score is 42,6854. Furthermore, a standard deviation value of 11,01573 was obtained which indicates that the environmental, social, and governance disclosure variables in this study have an even or consistent distribution of data due to the value of the mean obtained the largest value than the standard deviation value.

Table 3: Results of Descriptive Statistical Analysis

	N	Min	Max	Mean	Std. Dev
Tobin's Q	95	0,58	1,95	1,1667	0,3369 7
ROA	95	0,02	13,37	4,7992	3,2650 6
ESG Disclosure Score	95	24,6 2	69,12	42,685 4	11,015 73
Valid N (listwise)	95				

Classical Assumption Test

The data used in the study must go through a normality test to find out whether the residual or disruptive variables have a normal distribution of data or not (Ghozali, 2018). A regression model is said to be good if it shows a normal or near-normal distribution. The normality test also includes a graph probability plot, where the data is considered normal if it is scattered and follows around the diagonal line. In addition, other normality tests are operated in this test by using statistical tests One Sample Kolmogorov-Smirnov Test which meets the requirement that the data is normal if the probability of Asymp.Sig. (2-tailed) > 0,05 or 5%.

Table 4: Results of the Normality Test

One-Sample Kolmogorov-Smirnov Test			
		Unstandar dized Residual	Unstandar dized Residual
		Model 1	Model 2
N		95	95
Normal Parameter sa,b	Mean	0,0000000	0,0000000
	Std. Dev	0,1495668 8	3,2519412 3
Most Extreme Differences	Absolute	0,070	0,087
	Positive	0,070	0,087
	Negative	-0,055	-0,075
Test Statistic		0,070	0,087
Asymp. Sig. (2tailed)		0,200 ^{c,d}	0,070 ^c

Furthermore, regarding other classical assumption tests such as multicollinearity, heteroscedasticity, and autocorrelation, the results show that there is no evidence of multicollinearity, heteroscedasticity, or autocorrelation. As a result, the research data is suitable for further hypothesis testing.

Hypothesis Test Results

The Effect of Environmental, Social, and Governance Disclosure on Company Value

Based on Table 5 in model 1, the coefficient of ESG disclosure variables is measured using the ESG disclosure score. The results of the t-test found that the t-calculated and t-table values were 4,793 and 1,661, respectively, from the two results, showing that the t-calculated > t-table was 4,793 > 1,661 and the significance value was 0,000 < 0,05, so this number means that ESG disclosure has a significant influence on the company's value. In addition, the coefficient value in the ESG disclosure variable produces a positive influence of 4,793, which means that if there is an increase of 1% of ESG disclosure, it will provide an increase in the company's value of 4,793. Thus, the figure shows that environmental, social, and governance disclosure provides a positive direction of influence and has a significant influence on the increase in company value, so that H₁ is accepted.

The Effect of Environmental, Social, and Governance Disclosure on Profitability

Based on Table 5 in model 2, the coefficient of ESG disclosure variables is measured using the ESG disclosure score. The results of the t-test found that the t-calculated and t-table values were 5,339 and 1,661, respectively, from the two results, showing that the t-calculated > of the t-table was 5,339 > 1,661 and the significance value was 0,000 < 0,05, so this number means that ESG disclosure has a significant influence on profitability. In addition, the coefficient value of the ESG disclosure variable produces a positive influence of 5,339, which means that if there is an increase of 1% from ESG disclosure, it will provide an increase in profitability of 5,339. Thus, the figure shows that environmental, social, and governance disclosure provides a positive direction of influence and has a significant influence on the increase in profitability, so that H₂ is accepted.

Table 5: Results of Statistical Test t

	Type	Unstand. Coefficients		Stand. Coef	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1,067	0,014		74,618	0,000
	ESG Disclosure Score	0,465	0,097	0,447	4,793	0,000
2	(Constant)	4,801	0,042		112,984	0,000
	ESG Disclosure Score	0,543	0,102	0,490	5,339	0,000

Conclusion

ESG disclosure has a positive and significant effect on the company's value. This gives an indication that information disclosure through ESG disclosure directly plays an important role in increasing company value and investor confidence. Companies that actively disclose ESG practices demonstrate their commitment to sustainability, ethics, and social responsibility. This will have an impact on increasing the company's reputation and value in the eyes of consumers, investors, and the general public. In addition, the company will also increase investor interest and trust through transparent ESG disclosure as it will provide important information to investors regarding risks and opportunities related to environmental, social, and governance issues. Investors will increasingly recognize that good ESG performance can reduce risks and improve a company's performance in the long run.

ESG disclosure has a positive and significant effect on profitability. This gives an indication that information disclosure through direct ESG disclosure plays an important role in increasing the company's profitability. Companies that emphasize their commitment to sustainability through ESG disclosures can differentiate themselves in the market, thus influencing their reputation and public perception. Consumers who care about environmental and social issues are more likely to buy from companies that are considered socially responsible. A positive reputation fosters customer loyalty and trust, which leads to increased product demand and higher sales, which will ultimately increase the company's profitability.

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