The impact of environmental, social, governance (ESG) on financial performance (Empirical study of ASEAN firms listed on the Nikkei asia 300 index 2018 – 2022)

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Abstract
This research aims to determine the effect of disclosure of each ESG component on financial performance as proxied by ROA and ROE. This research also used control variables, namely Financial Leverage and Firm Size. This research used a sample of 37 ASEAN companies, including Indonesia, Malaysia, Singapore, Thailand, Philippines and Vietnam. The sampling technique used a purposive sampling method with secondary data obtained through Bloomberg. The number of observations in this study was 185 over a period of 5 years (2018 - 2022). Data analysis used multiple linear regression analysis of panel data and was assisted by Eviews 12 software. The findings from this research revealed that environmental disclosure and governance disclosure variables have a positive effect on ROA. Meanwhile, social disclosure has a positive effect on ROE. This research also reveals that environmental disclosure and governance disclosure has no effect on ROE, and social disclosure has no effect on ROA.

Keywords: Financial performance, environmental disclosure, social disclosure, governance disclosure, return on asset, return on equity

Introduction
Nowadays, firms are required for providing public accountability. Regarding to this, firms must report the forms of their accountability to maintain the trust of the community and stakeholders. Beside of financial report, firms are also required to provide its ESG report. ESG is a data-based framework and it focuses to investors (Winata, 2023) [32]. ESG report contains quantitative and qualitative informations related to 3 main components, that is environment, social, and governance. Nugroho and Haryanto (2023) [24] stated that the result of ESG performance's measurement are obtained from the sub-component ESG's average and subsequently becoming overall ESG. The higher the average ESG score of the firms, thus the better the firms' financial performance (Nugroho & Haryanto, 2023) [24].

Southeast Asia is one of economic alliances with the fastest GDP growth in the world (IMF, 2021)[16]. In recent years, the Southeast Asia region has attracted the attention of global investors. In 2018, ASEAN Capital Market Forum (ACMF) created the ASEAN Green Bond Standard that widely recognized and applied. This standard functioned as a framework for the creation of national green bonds or globally recognized standards.

However, the reality is only 6 countries in ASEAN that has obliged the ESG disclosure and the government gave the guidance to assist the issuers in providing sustainability informations (Sustain Analytics, 2021) [29]. These countries are Philippines, Singapore, Malaysia, Thailand, Vietnam, and Indonesia. Along with the importance of the concept of sustainability for many related parties, including society, investors, regulators, suppliers, shareholders and government agencies, therefore stakeholders realize the importance of firms' contributions such as performance in terms of environmental, social, and governance (ESG) (Al Amosh and Khotib, 2022) [2]. According to Goldstein and Yang (2017) [14], ESG components' disclosure considered the firms in order to achieve competitive market advantage and resulting in improved financial performance.

This study is referred on some previous studies regarding the impact of Environmental, Social and Governance (ESG) factors on financial performance. According to Nugroho and Hersugondo (2022) [23], ESG, EVN, SOC, and CG affect the financial performance significantly. ESG disclosure positively affects the financial performance. In addition, CSR negatively affects the financial performance.

Naeem, et al. (2022) [20] concluded that there is no statistically significant correlation between return on asset (ROA) in environmentally sensitive industries and ESG ratings. However, ESG performance score positively affects the return on equity (ROE). Additionally, Tobin's Q of environmentally sensitive industries obtain the advantages of evaluating ESG performance. Also, Rao, et al. (2023) [27] mentioned that the component of ROE and ESG have a significantly negative correlation. The research stated that the lower the ROE, the greater the Governance Pillar Score. However, Sandberg, et al. (2022) [28] claimed that in European food industries, there is a positive correlation between ESG on ROA and ROE. Kalia and Aggarwal (2023) [17] add that involving in ESG related activities positively and significantly affects financial performance that have been measured with ROA and ROE. In developed countries, every increase of 1 unit of a company's ESG assessment led to a 0.4% increase in ROA and ROE. Meanwhile, in developing countries, an increase of 1 ESG assessment unit led to an increase of 1.2% ROA and ROE.

Moreover, Al Amosh, et al. (2023) [2] argued that there is a positive correlation between environmental disclosure and ROA and disclose the environmental performance have an important role in increasing the market value. The findings indicated that social disclosure significantly affects the market value of the firm. Additionally, governance disclosure affects the profitability and has no effect on ROE. This research focuses on ASEAN firms because the firms in ASEAN countries has higher ESG risks than the companies in Europe and North America, and in line with the Asia Pacific average (Pan, 2021) [26]. In addition, many investors

believe that Southeast Asia, as one of the most important economic alliances in the world, has a prosperous future (Pan, 2021) [26].

Theoretical Perspectives, Framework, and Hypotheses Development

1. Stakeholder Theory

Stakeholder theory argues that by focusing analysis on the relationship between firms, groups, and individuals, then it can more effectively overcome those three problems. From a stakeholder's point of view, the company can achieve the goals that is defined as linkages between various groups that have an interests in company activities (Freeman, 1984) [11]. Firms are required to consider all the stakeholders' preference by fulfilling their needs without discrimination (Deegan & Blomquist, 2006) [7].

According to stakeholder theory, the activities related to CSR and disclosure activity provide the opportunity to the firms can demonstrate its efforts toward sustainability (Freeman *et al.*, 2004) [12]. Moreover, ESG information disclosure is beneficial for companies because it can raise awareness of ESG related issues in the society and help to explain environmental, social performance, and financial issues (Oncioiu *et al.*, 2020) [25]. Stakeholder theory provides the guidance for the firms in carrying out its operational activities.

2. Legitimacy Theory

Legitimacy theory states that there is a "social contract" that forces companies to ensure that their actions are acceptable according to social review by external parties, so this will legitimize their actions (Caesaria & Basuki, 2017) [6]. Legitimacy theory is seen as depending on community sensitivity in terms of giving legitimacy to the company (Al Amosh *et al.*, 2022) [2]. Similarly, managing sustainability activities influence stakeholder perceptions. Thus, supporting sustainability activities increase a company's legitimacy and acceptance in society. Conversely, neglecting sustainability activities can expand legitimacy gaps and threaten the corporate legitimacy (Al Amosh *et al.*, 2022) [2].

Nugroho and Haryanto (2023) [24] suggest that the legitimacy system societies affect and provide direct support to the sustainability of the company in carrying out its operational activities. The company strives to build credibility by involving in activities that demonstrate the fulfillment of environmental and social obligations to society. Such information may be disclosed by the company by publishing environmental and social information in company's annual report. Thus, this will be able to increase the companies' going concern in society.

3. Framework

This research framework is designed to improve cognitive processes in analyzing the issues discussed. This research is based on a conceptual framework, that is contained in the model below:
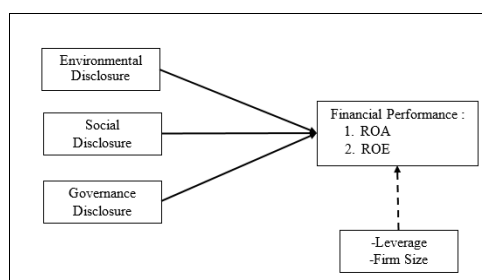

Fig 1: Framework

4. Hypotheses Development

The Impact of Environmental Disclosure on Financial Performance

Freeman (1984) [11] claimed that sharing information about environmental performance with stakeholders is a way to increase the success of the company. Regarding to stakeholder theory, investors and consumer's pressure have an important role in stimulating the environmental performance of the firms, which leads to maximizing the company's market value and viewing it more positively (Sutantoputra *et al.*, 2012) [30].

Several studies highlighted the influence of environmental disclosures on the company's financial performance. Khlif, *et al.* (2015) [18] provided evidence showing that environmental disclosure positively affects the performance in South Africa's companies. However, Alareeni and Hamdan (2020) [3] stated that environmental performance negatively affects ROE and ROA.

H1a : There is an impact of environmental disclosure on ROA

H1b : There is an impact of environmental disclosure on ROE

The Impact of Social Disclosure on Financial Performance

Nekhili, *et al.* (2017) [22] stated that corporate social responsibility disclosure has a significant role in determining the investment decisions of potential investors. Thus, social disclosure increases the likelihood of attracting more attention of stakeholders, mainly investors. Fisher-Vanden and Thorburn (2011) [10] revealed that social performance and financial performance have a negative relationship. Opposite with research by Khlif, *et al.* (2015) [18] that provided the social disclosure has a positive effect on financial performance of several companies in South Africa. Wasara and Ganda (2019) [31] also suggested that social disclosure has a positive effect on the financial performance of mining companies listed in Johannesburg. Meanwhile, Alareeni and Hamdan (2020) [3] stated that social performance negatively affects ROE and ROA.

H2a : There is an impact of social disclosure on ROA

H2b : There is an impact of social disclosure on ROE

The Impact of Governance Disclosure on Financial Performance

According to stakeholder theory, good governance is an important factor in improving financial performance, limit agency fees, and enable company to continue as a sustainable company (going concern) (Fama and Jensen, 1983) [8]. Several studies highlighted the influence caused by governance disclosure on financial performance of the firms. Klapper and Love (2004) [19] concluded that good governance improve financial performance. Bauer, *et al.* (2010) [5] also found that corporate governance has a positive impact on financial performance in real estate companies in the United States. In addition, Hussein and Kamardin (2016) [15] stated strong results associated with the positive relationship between corporate governance and financial performance of Fortune500 global companies (US and non-US). However, Al-Ahdal, *et al.* (2020) [1] stated

that governance disclosure have no significant effect on financial performance as measured by ROE and Tobin's Q. Meanwhile, the completed research Alareeni and Hamdan (2020) [3] stated that governance performance positively affects the financial performance.

H3a : There is an impact of governance disclosure on ROA

H3b : There is an impact of governance disclosure on ROE

Research Methodology
1. Population and Sample Selection
The population in this study used the multinational companies in ASEAN that listed on Nikkei Asia 300 Index over period 2018-2022. The number of companies listed on Nikkei Asia 300 Index as follows: 25 Indonesian companies, 22 Malaysia companies, 21 Singapore companies, 24 Thailand companies, 20 Philippines companies, and 5 Vietnam companies. The whole population used are 117 ASEAN companies. The sampling technique used a purposive sampling method with secondary data obtained through Bloomberg. This research used a sample of 37 ASEAN companies with the number of 185 observations.

2. Data Source
The data source that used in this research was secondary data. Regarding to this, secondary data refers to research data derived from indirect sources, such as annual reports, government publications or authoritative agencies, academic journals or literature, and others. The study was conducted by using secondary data in the form of: (1) Scientific journals obtained from publishers Scopus, Emerald, Springer, and Wiley; (2) ESG disclosure score index and its respective components from 2018 to 2022 obtained from Bloomberg Laboratories; and (3) annual report of companies listed on Nikkei Asia 300 Index from 2018 to 2022.

3. Data Collection and Analysis
This research was conducted using the study literature and documentation methods as methods for collecting data. This literature study method is obtained from reading academic journals and publications. Meanwhile, the documentation method, namely by collecting data from the company's official website and data from Bloomberg Laboratories. Data from the company's official website in the form of annual reports and ESG report. Bloomberg were used to obtain data about the ESG score index and its respective components. Data analysis was carried out using panel multiple regression analysis. The analysis method in this study was assisted by EViews 12 software.

4. Variable Measurements
This research used dependent variable, independent variable, and control variable. The variable dependent is financial performance that was proxied by ROA and ROE. In addition, the independent variable is ESG components, that is environmental disclosure, social disclosure, and governance disclosure. This research also used control variable, that is financial leverage and firm size. The variable measurements are presented in the following table :

Table 1: Variable Measurements

Variable	Measurement
Dependent Variable	
Return on Asset (ROA)	$\frac{Net\ Profit}{Total\ Assets} \times 100\%$
Return on Equity (ROE)	$\frac{Net\ Profit}{Total\ Equity} \times 100\%$
Independent Variable	
Environmental Disclosure	Bloomberg Index
Social Disclosure	Bloomberg Index
Governance Disclosure	Bloomberg Index
Control Variable	
Financial Leverage	$Ln(\frac{Total\ Liability}{Total\ Equity})$
Firm Size	Ln(Total Assets)

5. Research Model
Panel multiple regression analysis was used with the aim to test the effect of two or more independent variables against one dependent variable (Ghozali and Ratmono, 2020) [13]. Regarding to this, the model

commonly used in panel multiple regression analysis is the ordinary least square (OLS) method. Regression equation model in this research is formulated as follows:

Model 1 :
$$ROA = \alpha + \beta1ENV + \beta2SOC + \beta3GOV + \beta4FLEV + \beta5FSIZ$$

Model 2 :
$$ROE = \alpha + \beta1ENV + \beta2SOC + \beta3GOV + \beta4FLEV + \beta5FSIZ$$

Where
ROA = Return on Asset
ROE = Return on Equity
ENV = Environmental Disclosure
SOC = Social Disclosure
GOV = Governance Disclosure
FLEV = Financial Leverage
FSIZ = Firm Size
α = constanta
β1- β5 = Coefficient Regression

Analysis and Results
1. Descriptive Statistics
Table 2 shows the descriptive statistics result for each dependent variable, independent variable, and control variable of the research. ROA has a minimum value of -0.59% and maximum value of 8.00% with the average of 2.589%. The standard deviation of ROA is 1.7798% and it means that the data used in this research are not very diverse.
ROE has a minimum value of -6.57% and maximum value of 22.14% with the average of 9.8507%. The standard deviation of ROE is 4.8109% and it means that the data used in this research are not very diverse.
ENV has a minimum value of 0.00 and maximum value of 86.10 with the average of 34.6977. The standard deviation

of ENV is 18.5812 and it means that the data used in this research are not very diverse.

SOC has a minimum value of 0.00 and maximum value of 68.86 with the average of 33.2589. The standard deviation of SOC is 12.2329 and it means that the data used in this research are not very diverse.

GOV has a minimum value of 38.38 and maximum value of 96.12 with the average of 82.9723. The standard deviation of GOV is 11.3546 and it means that the data used in this research are not very diverse.

According to the control variable, the natural logarithm of FLEV has minimum value of 1.53 and maximum value of 5.66 with the average 4.3942. In addition, the natural logarithm of total assets has a minimum value of 20.57 and maximum value of 27.04 with the average of 23.9716.

Table 2: Descriptive Statistics

	N	Min	Max	Mean	Median	Std. Dev
ROA	185	-0.59	8.00	2.589	2.2612	1.7798
ROE	185	-6.57	22.14	9.8507	9.5471	4.8109
ENV	185	0.00	86.10	34.6977	33.3132	18.5812
SOC	185	0.00	68.86	33.2589	31.3785	12.2329
GOV	185	38.38	96.12	82.9723	87.357	11.3546
FLEV	185	1.53	5.66	4.3942	4.4530	0.7016
FSIZ	185	20.57	27.04	23.9716	23.73	1.4802

Source : Processed Data, 2024

2. Classic Assumption Tests

Table 3, table 4, and table 5 shows each of multicollinearity test, heteroscedasticity test, and autocorrelation test.

Table 3: Multicollinearity Tests

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
ENV	4.15E-05	7.391510	1.640385
SOC	8.88E-05	12.84050	1.522819
GOV	9.69E-05	78.32962	1.432321
FLEV	0.020564	46.91727	1.160364
FSIZ	0.004710	313.0405	1.182771

Source : Processed Data, 2024

Table 4: Heteroscedasticity Tests

Model	Variable	Probability
1	ENV	0.2882
	SOC	0.8345
	GOV	0.4664
	FLEV	0.2003
	FSIZ	0.3636
2	ENV	0.1792
	SOC	0.0694
	GOV	0.1942
	FLEV	0.5282
	FSIZ	0.1394

Source : Processed Data, 2024

Table 5: Autocorrelation Tests

Model	K	0<	DW<	DL
1	3	0	1.353	1.7266
2	3	0	1.096	1.7266

Source : Processed Data, 2024

According to table 3, it indicates the VIF (Variance Inflation Factors) value of all the independent variables and control variables are shown in Centered VIF < 10. The VIF of the

ENV is 1.640385, the SOC is 1.522819, the GOV is 1.432321, FLEV is 1.160364, and FSIZ is 1.182771. According to the results of the multicollinearity test, it can be concluded that there is no multicollinearity among independent variables.

Meanwhile, table 4 shows the heteroscedasticity test result. In the Glejser Test, when the probability value > 0.05, there is no heteroscedasticity. Regarding table 4, it shows that the probability value of Glejser Test In model 1 for the whole variable is more than 0.05. The probability value in model 2 for the whole variable is also more than 0.05. So, it can be concluded that in both model 1 and model 2, there is no heteroscedasticity.

Moreover, table 5 indicates that the Durbin-Watson value of ROA (model 1) is 1.374 and ROE (model 2) is 1.089. Result shows that the Durbin-Watson value is between 0 and DL (0 < DW < DL). Thus, the Durbin-Watson test result revealed that there is a positive autocorrelation in the research model. However, basically, autocorrelation is only intended for time series data (Napitupulu *et al*., 2021)[21]. Ghozali and Ratmono (2020)[13] also stated that in addition to time series data, the symptoms of autocorrelation very rarely happen because different residuals begin if it originates from different groups.

3. Hypotheses Test Result

Table 6 and table 7 shows the result of t statistic Test and determination coefficient test.

Table 6: t Tests Result

Dependent Variable	Independent Variable	Coefficient	Std. Error	t-Statistic	Probability
ROA	ENV	0.0022134	0.006439	3.437710	0.0007
	SOC	0.001335	0.009423	0.141626	0.8875
	GOV	0.021823	0.009846	2.216564	0.0279
	FLEV	-0.715378	0.143403	-4.988592	0.0000
	FSIZ	-0.780135	0.068627	-11.36769	0.0000
ROE	ENV	-0.019970	0.023108	-0.864205	0.3886
	SOC	0.091081	0.033818	2.693227	0.0077
	GOV	0.056573	0.035335	1.601057	0.1111
	FLEV	-1.589533	0.514664	-3.088488	0.0023
	FSIZ	0.028879	0.246299	0.117253	0.9068

Source : Processed Data, 2024

Table 7: Coefficient of Determination Tests

Model	R-squared	Adjusted R-squared	S.E. of regression
1	0.506958	0.493186	1.267075
2	0.130804	0.106525	4.547453

Source: Processed Data, 2024

Table 6 shows the Prob(t-statistic) values for ROA (model 1), it revealed that the probability value for ENV and GOV variable < 0.05. Meanwhile, the probability value of the SOC variable > 0.05. Based on this, hence ROA is only affected by ENV and GOV. SOC variables have no effect on ROA. Therefore, it can be concluded that the H1a and H3a hypothesis were accepted, but H2a was rejected.

Table 6 also shows that Prob(t-statistic) value for ROE (model 2), it revealed that probability value for SOC variable < 0.05. Meanwhile, the probability value of ENV and GOV variables > 0.05. Therefore, ROE is only affected

by SOC. ENV and GOV variables are not effect on ROE. Thus, it can be concluded that the H1b and H3b hypothesis were rejected, but H2b was accepted.

Additionally, according to the table 7, the results of the coefficient of determination testing indicates that the adjusted R-squared value for model 1 is 0.4931, it means that as much as 49.31% of ROA variables (model 1) can be explained by the independent variables ENV, SOC, and GOV. Meanwhile, the residual value is 50.69% (100% - 49.31%) has been explained by several other variables outside the model. Moreover, coefficient of determination testing for ROE (model 2) indicates that the adjusted R-squared value for model 2 is 0.1065, it means that as much as 10.65% of ROE variable can be explained by the independent variables ENV, SOC, and GOV. Meanwhile, the residual value is 89.35% (100% - 10.65%) has been explained by some other variable outside the model.

Based on the hypothesis testing, it showed that environmental disclosure positively affects the ROA. These findings are in line with Al Amosh, *et al.* (2022) [2] and Kalia and Aggarwal (2023) [17]. Every increase of 1 ENV score, then ROA will increase by 0.022%. Assumption of environmental disclosure are influentially positive for ROA is that the company is able to reduce its costs issued in addressing environmental impacts. The company is considered capable in managing waste and emissions, so that they do not cause environmental pollution. Because the company has succeeded in reducing costs to maintain the environment, then the company is able to generate profits that tend to be constant.

The hypothesis testing also indicates that environmental disclosure has no effect on ROE as stated by Rao, *et al.* (2023) [27]. Assumption of environmental disclosure has no effect against ROE is that based on environmental disclosure score data, there are several companies that have a score below 50. Fiori, *et al.* (2011) [9] stated that investors tend to consider the company which pays attention to environmental activities. There are still many ASEAN companies that got an environmental disclosure score < 50 leads to less investors interested in investing and the company's ROE in the absence of a significant changes.

Furthermore, the results show that social disclosure has no effect on ROA. It agreed with the results of Naeem, *et al.* (2022) [20]. Assumption that social disclosure has no effect on ROA is that social activities carried out by companies require a lot of resources, which can increase the financial expenses of the company. Therefore, the company tends to spend more funds on social activities that can lower ROA. In contrast, social disclosure positively affects the ROE. These results support the evidence stated by Naeem, *et al.* (2022) [20]. Every increase of 1 SOC score, then ROE will increase by 0.091%. Assumption of social disclosure positively affects the ROE is that the company is able to take responsibility in meeting the social satisfaction of stakeholders and the company successfully have good relations with external parties. CSR disclosure has an important role in determining the investment decisions of potential investors. Thus, social disclosure will increase the likelihood to attract more investors' attention to make investments that can be able to increase ROE.

Moreover, table 6 also shows that governance disclosure positively affects the ROA as in line with Alareeni and Hamdan (2020)[3]. Every increase of 1 GOV score, then the ROA will increase by 0.021%. Assumption of governance

disclosure positively affects ROA is that company's management can make good decisions, so that the company can continue to compete amid the onslaught of ESG issues. Good decision making, especially capital raising decisions, increased investment, budgeting, and asset management capabilities lead to good financial performance.

However, governance disclosure has no effect on ROE. These findings agreed with Al Amosh, *et al.* (2022) [2]. Assumption of governance disclosure has no effect on ROE is that governance-related activities are activities for internal company. Investors and external parties put more emphasis on activities related to the environment and social that directly attract the interest of external parties.

Relating to variable controls, the findings revealed that companies' financial leverage affects its ROA and ROE, while the firm size only affects its ROA and has no effect on ROE.

Conclusions, Limitations, and Future Research
1. Conclusions
The results show that environmental disclosure and governance disclosure positively affects the ROA. Every increase of 1 ENV score, the ROA will increase by 0.022%, while every increase of 1 GOV score, the ROA will increase by 0.021%. However, only social disclosure that positively affects the ROE. Based on hypothesis testing, every increase of 1 SOC score, the ROE will increase by 0.091%.

This research revealed findings that ASEAN companies are less sensitive to ESG issues. According to Sustain Analytics (2021) [29], only 6 countries in ASEAN have required ESG disclosures and governments provide guidelines to help issuers prepare sustainability information. Other than that, there are ASEAN companies that obtained low scores in their ESG components' disclosure.

2. Limitations
This research meets several limitations, such as the small research sample due to the large number of companies in ASEAN that do not disclose their full ESG performance. Subsequently, in the research model, there is an autocorrelation caused by successive observations or can be made on all the time interrelated (Ghozali and Ratmono, 2020) [13]. Also, this research only focused on companies' financial performance, while there are many other focuses related to ESG activities.

3. Future Research
Future research can expand the sample and compare with developed countries that pay more attention to ESG issues. Additionally, it can use other indexes, such as the Nifty 50 Index or the National Stock Exchange (NSE). Second, it can focus on the mining sector, food production, and healthcare companies that tended to be more sensitive to ESG. Data does not only obtained through Bloomberg, but also Thompson Reuters and Refinitiv Eikon. Third, autocorrelation in panel data is legitimate because autocorrelation essentially is only intended for time series data (Napitupulu *et al.*, 2021) [21]. Future research also can look for variables other than financial performance, such as working capital and Gross Profit Margin (Al Amosh *et al.*, 2022) [2].

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