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# DOES ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) DISCLOSURE LEAD TO GREATER FIRM VALUE? UNVEILING THE MEDIATING ROLE OF FINANCIAL PERFORMANCE

**HENDI ROHENDI***
**YETI APRILIAWATI**

Politeknik Negeri Bandung
Jalan Gegerkalong Hilir, Ds Ciwaruga, Kec. Parongpong, Kab. Bandung Barat, West Java Province, Indonesia

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**Corresponding author:**
hendi.rohendi@polban.ac.id

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***Abstract***: *Previous empirical findings on the relationship between ESG disclosure and firm value have shown inconsistent results. Some studies suggest that ESG disclosure enhances firm value, while others view it as a cost burden or a managerial tool used for personal gain. These inconsistencies create uncertainty for stakeholders in making economic decisions and indicate that previous theoretical models may be incomplete. Addressing this gap, the current study introduces a new approach by incorporating financial performance as a mediating variable in the relationship between ESG disclosure and firm value. This study utilized panel data from 51 companies listed on the Indonesia Stock Exchange, covering the period from 2015 to 2022, with a total of 357 firm-year observations. Hypothesis testing was conducted using the PLS–SEM methodology through the WarpPLS 8.0 software. The results indicate that ESG disclosure does not have a significant direct effect on firm value. This study has three contributions. First, it provides an answer to previous studies showing inconsistent directions. Second, the outcomes lend support to the proposition that financial performance bridges the influence of ESG disclosure on firm value. Third, it provides an understanding to company managers that ESG disclosure is important to improving financial performance. The implications of this research indicate that ESG disclosure can be incorporated as a strategy to improve financial performance and indirectly strengthen firm value.*
**Keywords:** ESG, financial performance, firm value, leverage, size

## INTRODUCTION

In the last five decades, firm value has become the center of attention of stakeholders and shareholders. When the firm value is not optimal, companies try to find a solution to enhance it (Husnan, 2014). Firm value can be seen as investors' assessment of a company. This assessment is fundamental, considering that the value of a company serves as an indicator of the potential future returns to its shareholders. Therefore, it is reasonable to assert that firm value plays a crucial role in supporting the broader objective of corporate sustainability.

Despite its essential role in company sustainability, the phenomenon that occurs with firm value in Indonesia from 2015 to 2022 shows fluctuating, even decreasing, trends (Harun et al., 2020). This is reinforced by data regarding firm value projected with Tobin's Q in the period from 2015 to 2022, which experienced a decline, as is the case with PT. Bumi Serpong Damai, PT. Pembangunan Perumahan, PT. Gudang Garam, and PT. AKR Corporindo.

Given its the importance, academic researchers and practitioners seek to help companies achieve optimal firm value. Several strategic steps have been taken to do so, one of which is to harness the role of ESG disclosure, which has been found to have an impact on increasing firm value (Abdi et al., 2021; Behl et al., 2021; Chauhan & Kumar, 2018; Feng & Wu, 2021; Thahira & Mita, 2021; Zumente & Bistrova, 2021).

ESG disclosure refers to the reporting of company initiatives and performance in the areas of environment, social responsibility, and governance (Ali et al., 2015; Lee et al., 2022). The environmental aspect consists of resources, emissions, innovation, and firm recycling performance, and it concerns environmental issues such as waste disposal, greenhouse gas emissions, climate-related risks, and other ecological effects. The social aspect addresses issues such as human rights, labor conditions, community involvement, product responsibility, and social contributions, with the goal of fostering stakeholder confidence and commitment (Albitar & Gerged, 2020). Meanwhile, the governance aspect includes management and shareholder welfare, corporate commitment, and organizational effectiveness in implementing corporate governance principles (Peng & Isa, 2020).

ESG disclosure makes a positive contribution, providing benefits such as being a communication medium between stakeholders and management (Gamayuni, 2015), improving ethical behavior (Dkhili, 2023), creating a positive impression (Uyar et al., 2020), enhancing organizational performance assessment (Lahouel et al., 2020), and providing positive signals to stakeholders (Bardos et al., 2020; Iatridis, 2013; Thahira & Mita, 2021; Yordudom & Suttipun, 2020).

ESG disclosure sends positive signals, motivating stakeholder involvement and thus potentially driving up the company's value. Such signaling occurs because stakeholders do not always have access to internal information, which may be perceived as either good or bad news (Lu & Wang, 2021; Su et al., 2016). Theory on signaling offers insights into the actions taken by individuals or organizations in reaction to information disclosure (Ellili, 2022).

Voluntary disclosure helps reduce information asymmetry between firms and stakeholders (Bianchi et al., 2010; Coleman et al., 2010).This is because disclosure will make information, which was previously only known to the company, available to investors and stakeholders, and thus become useful for them (Assidi, 2020). In addition, as companies operate in ever-changing environments, repeated disclosure helps mitigate information asymmetry even further (Eliwa et al., 2019). Therefore, disclosing ESG-related information can convey a positive signal to investors, potentially leading to an increase in firm value.

Empirical evidence from earlier studies suggests that ESG disclosure enhances firm value, but another group of researchers showed contradictory results (Rohendi et al., 2024). From the perspective of some investors, ESG disclosure is seen as a cost rather than a value-generating investment. In fact, in some cases, it functions as a managerial tool for enhancing personal value rather than organizational performance. In addition, several studies reported that ESG disclosure and firm value do not have a significant relationship (Yoon et al., 2018). They are of the view that there are other factors that can increase firm value. Therefore, they stated, ESG disclosure could not provide a positive signal for increasing firm value.

Inconsistent results of previous studies can confuse stakeholders in their economic decision making (Wang et al., 2016). Hair et al. (2017) stated that when there were inconsistencies in previous research, it is possible that there were variables not included in the model (omitted variables). In other words, there is the possibility that the theoretical model built in previous research was incomplete. Identifying mediating variables may play a key role in clarifying how independent variables affect the dependent variable. In view of the existing literature gap, the current study seeks to enhance the existing model and provide a more comprehensive explanation of the relationship between ESG disclosure and firm value by examining the indirect influence of other intervening mechanisms on this interaction.

The variable that is thought to intervene in this relationship is financial performance. In literature, it is stated that one of the reasons companies disclose ESG information is to improve their financial performance (Brooks & Oikonomou, 2018; Song et al., 2020) and subsequently provide a positive signal to stakeholders, which may ultimately enhance their firm value. Therefore, the current study is novel compared to previous research as it explored the role of financial performance as a mediating variable between ESG disclosure and firm value. The research specifically looked at Indonesian firms listed on the Indonesia Stock Exchange, in consideration that their operations may have detrimental effects on society and the environment. Furthermore, it has been recognized that despite the suboptimal state of ESG disclosure in Indonesia, notable progress has been made, as indicated by the Indonesia Stock Exchange's participation in the United Nations Sustainable Stock Exchange (SSE) Initiative since 2019.

This study is important because it has three contributions. First, it is able to provide an answer to previous studies showing inconsistent directions. Second, it provides new evidence that financial performance can act as a mechanism that mediates the impact of ESG disclosure on firm value. Third, it provides an understanding to company managers that ESG disclosure is important to improving financial performance.

## THEORETICAL FRAMEWORK AND HYPOTHESES

### The Effect of ESG Disclosure on Firm Value

Information disclosure is crucial for a company because it allows stakeholders to understand the company's condition better and thus affects their decision making (Thahira & Mita, 2021). One of the most important pieces of information that companies should disclose to stakeholders is information on ESG. Disclosing ESG information can encourage investors to invest due to reduced information asymmetry (Yordudom & Suttipun, 2020), increased company transparency and comparability (Feng & Wu, 2021), and better efficiency (Abdi et al., 2021). These various benefits of ESG disclosure will send a positive signal to the various parties involved, encouraging them to take part in contributing to the company, hence the company's increased value.

Voluntary disclosure of information serves as an effective mechanism to reduce information asymmetry between firms and their stakeholders (Bianchi et al., 2010). This is because this information is only known t the company, and making it available to investors and stakeholders will bring benefits (Tischer & Hildebrandt, 2014). This information asymmetry can be reduced further by the company by providing this information repeatedly, especially as the company operates in an highly dynamic environment (Eliwa et al., 2019). Information disclosure, such as ESG disclosure, can provide a positive signal and have a much better impact on firm value, in line with previous research (Aboud & Diab, 2019; Chauhan & Kumar, 2018; Faisal et al., 2020; Gerged at al., 2021). Thus, the hypothesis below was proposed:

$H_1$: ESG disclosure has a positive effect on firm value.

### The Effect of ESG Disclosure on Financial Performance

Financial performance has an important role for external parties to a company, as it allows them to assess and monitor the way in which the company carries out their activities to generate profits from the assets in its disposal. Stakeholder theory states that companies should not only pay attention to profits, but must also pay attention to stakeholder rights, which are related to the extent to which the companies care about their social management and corporate governance. As stated by Tu & Huang (2015), a harmonious relationship between companies and stakeholders can be built by the companies by disclosing activities related to ESG.

According to Ahmad et al. (2021), when a company fully discloses ESG, its financial performance will be better, because it indicates that the company has received evaluation from the public, which contributes to the company's growth. Besides, Fahad & Busru (2020) reviewed 80 articles for the relationship between social and environmental responsibility and financial performance and found that more than half of them provided empirical evidence in the direction of a positive relationship. The current study examined the relationship between ESG disclosure and financial performance in Indonesia, which is characterized by sub-optimal ESG disclosure, using a wider sample, which included both financial and non-financial companies. On this link, the hypothesis below was proposed:

$H_2$: ESG disclosure has a positive effect on financial performance.

### The Effect of Financial Performance on Firm value

Financial performance refers to a company's ability to generate profits from the total assets in its possession. Good financial performance reflects that the company is effective in managing its operations. In addition, it can be an indicator of the company’s prospect for growth and development (Summit, 2001). Furthermore, good company financial performance can contribute positively to firm value, as it encourages investors to invest. It is consistent with signal theory, which states that firm value can increase when there are positive signals given by stakeholders and shareholders to the company, which in this case is shown by their willingness to invest (Bardos et al., 2020; Yordudom & Suttipun, 2020). This is due to the formation of a good reputation, transparency, and a good profile of the company (Iatridis, 2013).

Previous research supports financial performance’s positive impact on firm value (Gharaibeh, 2018; Nuryaman, 2015). Kiprono et al. (2024) stated that when a company wants to get high firm value, the share price should be high, and this can be achieved when the company's financial performance is good. Based on this description, it was hypothesized that:

$H_3$: Financial performance has a positive effect on firm value.

**The Mediation of Financial Performance in the Relationship between ESG Disclosure and Firm Value**

Financial performance reflects a company's ability to manage its business activities effectively and efficiently, both in the short and long terms. One of the strategic measures that the company can take to enhance its financial performance is to engage in ESG disclosure. ESG disclosure demonstrates the company's commitment to sustainable business practices and its responsiveness to stakeholder concerns related to environmental protection, social responsibility, and good governance. This disclosure is not merely symbolic; it represents a proactive stance toward long-term value creation and risk management.

Companies that engage in ESG disclosure tend to attract positive attention from investors, customers, and regulators, thereby improving stakeholder trust and corporate legitimacy (Duque et al., 2019). This increased stakeholder confidence can, in turn, translate into tangible financial benefits, such as enhanced sales, lower operational and reputational risks, improved employee productivity, and access to cheaper financing. As highlighted by previous studies, ESG disclosure is believed to positively influence financial performance due to these cumulative benefits, particularly in strengthening stakeholder relationships.

Improved financial performance serves as a critical intermediary mechanism that helps transform non-financial initiatives like ESG disclosure into financial value. When a company demonstrates strong financial results, measured through profitability, efficiency, or return on assets, it sends a positive signal to investors and market participants. This signal can shape market perceptions of the firm's prospects, risk profile, and managerial competence. As a result, stronger financial performance increases investor confidence, enhances market valuation, and contributes to higher firm value. This link between financial performance and firm value has also been confirmed by previous studies, which suggest that financial metrics are key drivers of shareholder wealth maximization (Haninun et al., 2018; Gatimbu & Wabwire, 2016; Nor et al., 2016; Song et al., 2020).

In summary, ESG disclosure can be seen as an upstream driver of improved financial outcomes, which then function as a downstream determinant of firm value. Financial performance, therefore, acts as a mediating variable that explains how and why ESG disclosure may ultimately influence firm value. Therefore, the hypothesis developed for this interaction is that:

$H_4$: Financial performance positively mediates the relationship between ESG disclosure and firm value.

## RESEARCH METHODS

In an effort to better understand the interplay between sustainability practices and corporate valuation, this study employed a quantitative explanatory approach. It delved into how ESG disclosure relates to firm value and explored the dual role of financial performance, not only as a standalone predictor but also as a mediator. The investigation spanned a broad selection of companies listed on the Indonesia Stock Exchange, encompassing both financial and non-financial entities. Meanwhile, the sample consisted of 357 observations for the period from 2015 to 2022. Table 1 outlines the sample distribution of 51 Indonesian companies covering the years 2015 to 2022.

Table 1. Sample Distribution

| Description | Amount |
|---|---|
| Companies listed on the Indonesian market that reported on ESG for the period from 2015 to 2022 | 79 |
| Minus: incomplete data | (28) |
| Sample of selected companies | 51 |
| Total observations (51 × 7) | 357 |

Source: Bloomberg database, 2024

In this study, firm value served as the dependent variable and was measured using Tobin's Q. This metric was calculated as (Market Capitalization + Total Liabilities + Preferred Equity + Minority Interest) / Total Assets, providing a comprehensive indicator of a firm's market valuation relative to its asset base. The use of this measurement approach is well-established in the existing literature (Aboud & Diab, 2018; Feng & Wu, 2021; Rohendi et al., 2024).

Furthermore, in this study, ESG disclosure served as an independent variable, measured using the content analysis method. The ESG disclosure score was determined by assigning a value of 1 to each disclosed indicator component and 0 to those not disclosed, based on data from the Bloomberg database. This measurement has been carried out by previous researchers as well (Behl et al., 2021; Huang et al., 2022; Qiu et al., 2016; Rohendi et al., 2024). In addition, financial performance was used as a mediating variable and was measured through ROA. The formula used for financial performance was ROA = Net Income / Total Assets.

This research included size and leverage as control variables. Firm size refers to the scale of a company, which can influence its capacity to disclose ESG-related information due to the availability of resources (Drempetic et al., 2020). The operations in larger firms are broader in scope, and they exert a more substantial impact on the community (Milne et al., 2016). Meanwhile, leverage was applied as a control variable to oversee the company's capital structure, which has a significant connection to ESG disclosure issues. In prior studies, leverage has been recognized as a key factor when assessing the influence of ESG disclosure on firm value (Chauhan & Kumar, 2018; Feng & Wu, 2021; Yiwei et al., 2018). The research model used in the current study is shown in Figure 1.

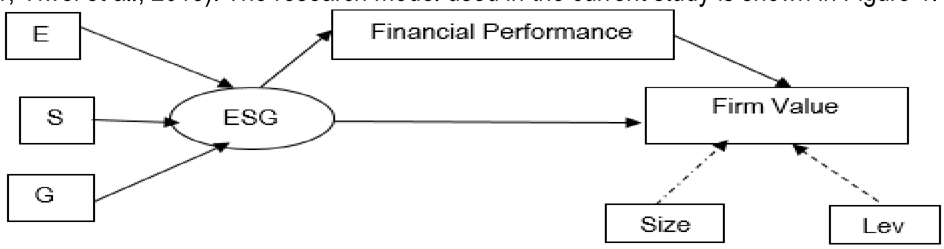


Figure 1. Research Model

The following outlines the specifications of the research model used to test hypotheses based on the proposed framework:

Fin. Perf = $\beta_1$ESG + $e_1$ ............................................................................................................ (1)

$FV_{it+1}$ = $\beta_2$ESG + $\beta_3$FP + $\beta_4$Size + $\beta_5$Leverage + $e_2$............................................................. (2)

Analysis in this research was conducted using PLS–SEM, because it included first-order formative–formative construct variables, which cannot be analyzed with CB–SEM (Schabek, 2020). The PLS–SEM analysis was carried out in two distinct phases: the first phase evaluated the measurement model to validate the ESG construct through its indicators, while the second phase focused on assessing the structural model to test the proposed relationships between variables (Hair et al., 2017).

## RESULTS AND DISCUSSION

Table 2 shows the descriptive statistics of all the estimated variables.

Table 2. Descriptive Statistics

| Variables | Mean | Std Deviation | Minimum | Maximum |
|---|---|---|---|---|
| FV | 1.547353 | 1.175973865 | 0.5548 | 9.7012 |
| Fin. Perf | 4.98985 | 7.881495642 | -16.6274 | 7.881495642 |
| E | 0.362306315 | 0.292896264 | 0 | 0.928571429 |
| S | 0.505142862 | 0.214621245 | 0 | 0.952380952 |
| G | 0.723024915 | 0.120784118 | 0.37037037 | 0.95003 |
| ESG | 0.529926376 | 0.18442002 | 0.148148148 | 0.866843034 |
| Size | 31.44785517 | 1.511910353 | 27.07602299 | 35.08435768 |
| Lev | 0.550463001 | 0.223845481 | 0.120634726 | 0.944663971 |

Source: Bloomberg database, 2024

Table 2 shows an average ESG disclosure score of 52.992, which reflects a moderate level of transparency among Indonesian companies. It indicates that, on average, only half of the relevant ESG information was disclosed. The maximum score of 86.68 indicates that companies were highly committed to ESG reporting. When broken down by dimension, governance disclosure ranked highest at 72.30, followed by social disclosure at 50.514 and environmental disclosure at 36.230. These findings highlight the environmental component as the weakest area, which requires greater attention from companies operating in Indonesia.

Furthermore, the mean for financial performance was 4.98985, which means that the level of return on the assets owned by an average company was relatively high. Thus, it can be said that companies in Indonesia were very efficient in generating operating profits from their assets. The mean for firm value was 1,547, above the threshold of 1. Therefore, it can be said that companies in Indonesia were optimal in generating firm value, because the market value of their assets exceeded their replacement cost (Kaijser, 2014). The average firm size was 31.447, while the average leverage was 0.5504, indicating that about half of the asset financing came from debt.

Table 3 shows the validity of the formative constructs that shaped ESG disclosure. The *p*-value of ESG disclosure was below 0.05, and the VIF value was ≤ 3.3. This means that the model in this research was free from symptoms of multicollinearity. In other words, the formative constructs forming ESG disclosure met the validity requirements.

Tabel 3. Output Indicator Weight

| Indicator | ESG | Performance | NP | Size | Lev | Type of Indicator | SE | *p*-Value | VIF | S |
|---|---|---|---|---|---|---|---|---|---|---|
| E | (0.423) | 0.000 | 0.000 | 0.000 | 0.000 | Formative | 0.050 | 0.001 | 2.977 | 0.325 |
| S | (0.425) | 0.000 | 0.000 | 0.000 | 0.000 | Formative | 0.050 | 0.001 | 3.014 | 0.388 |
| G | (0.325) | 0.000 | 0.000 | 0.000 | 0.000 | Formative | 0.051 | 0.001 | 1.273 | 0.227 |
| ROA | 0.000 | (1.000) | 0.000 | 0.000 | 0.000 | Formative | 0.046 | 0.001 | 0.000 | 1.000 |
| Q | 0.000 | 0.000 | (1.000) | 0.000 | 0.000 | Formative | 0.046 | 0.001 | 0.000 | 1.000 |
| Size | 0.000 | 0.000 | 0.000 | (1.000) | 0.000 | Formative | 0.046 | 0.001 | 0.000 | 1.000 |
| Lev | 0.000 | 0.000 | 0.000 | 0.000 | (1.000) | Formative | 0.046 | 0.001 | 2.977 | 0.325 |

Source: WarpPLS 8.0 output, 2024

Table 4 shows the feasibility of the model built in the research. This evaluation was carried out by examining the indicators presented in the table.

Tabel 4. Model Goodness of Fit

| Model Fit and Indices Quality | Fit Criteria | Analysis Results | Description |
|---|---|---|---|
| *Average path coefficient (APC)* | $p \leq 0.05$ | 0.226 ($p <$ 0.001) | Qualified model fit |
| *Average R-squared (ARS)* | $p \leq 0.05$ | 0.322 ($p <$ 0.001) | Qualified model fit |
| *Average adjusted R-squared (AARS)* | $p \leq 0.05$ | 0.319 ($p <$ 0.001) | Qualified model fit |
| *Average block VIF (AVIF)* | Accepted, if ≤ 5, ideal ≤ 3.3 | 1.257 | Ideal |
| *Average full collinearity VIF (AFVIF)* | Accepted, if ≤ 5, ideal ≤ 3.3 | 1.596 | Ideal |
| *Tenenhaus GoF (GoF)* | Small ≥ 0.1, medium ≥ 0.25, large ≥ 0.36 | 0.551 | Large |
| *Sympson's paradox ratio (SPR)* | Accepted if ≥ 0.7, ideal = 1 | 1.000 | Ideal |
| *R-squared contribution ratio (RSCR)* | Accepted if ≥ 0.9, ideal = 1 | 1.000 | Ideal |
| *Statistical suppression ratio (SSR)* | Accepted if ≥ 0.7 | 1.000 | Accepted |
| *Nonlinear bivariate causality direction ratio (NLBCDR)* | Accepted if ≥ 0.7 | 1.000 | Accepted |

Source: WarpPLS 8.0 output, 2024

According to Table 4, it is evident that the model established in this study had good fit, as reflected in every indicator examined. The value for the APC indicator was 0.226, while the fit criterion was that *p*-value = 0.001 ≤ 0.05, implying that the model aligned with the criterion for a well-fitting model. Likewise, the ARS indicator value of 0.322, with *p*-value = 0.001 ≤ 0.05, indicates that it met the criterion for a fit model. The AARS value was 0.319, implying that the model aligned with the criterion for a well-fitting model. Furthermore, the model had AVIF and AFVIF of 1,257 and 1,596, respectively, below the 3.3 threshold for an ideal model. Therefore, it is concluded that the model was ideal and free from symptoms of multicollinearity. Additionally, a GoF value of 0.551 (≥ 0.36) implies that the model built fell within the strong category. Finally, the indicators for SSR, NLBCDR, RSCR, and SPR had the same value, namely, 1.000, which shows that the model was ideal and free from causality problems.

Table 5 displays the findings from the assessment of the structural model created in this study. The goal of this analysis was to investigate the causal relationships between variables, based on an established theoretical foundation.

Table 5. Evaluation of the Model Structure

| | ESGD | Fin Perf | FV | Size | Lev |
|---|---|---|---|---|---|
| R-Squared | | 0.041 | 0.604 | | |
| Adj. R-Squared | | 0.038 | 0.599 | | |
| Composite reliability | 0.882 | 1.000 | 1.000 | 1.000 | 1.000 |
| Cronbach's alpha | 0.795 | 1.000 | 1.000 | 1.000 | 1.000 |
| Average var. extracted | 0.716 | 1.000 | 1.000 | 1.000 | 1.000 |
| Full collinearity VIFs | 1.088 | 1.987 | 1.882 | 1.544 | 1.539 |
| Q-squared | | 0.041 | 0.574 | | |
| Min | -2.293 | -2.743 | -0.844 | 2892 | 1920 |
| Max | 1.778 | 5.555 | 6.934 | 2.405 | 1.761 |
| Median | 0.000 | 0.0234 | -0.323 | -0.097 | -0.133 |
| Mode | 0.000 | -0.561 | -0.609 | 0.674 | 1.129 |
| Skewness | -0.210 | 2.111 | 3.800 | 0.009 | -0.036 |
| Exc. Kurtosis | -0.975 | 8.552 | 18.305 | 0.674 | 1.129 |

Source: WarpPLS 8.0 output, 2024

The R-Squared value of 0.604 indicates that ESG disclosure and financial performance together explained 60% of the variation in firm value, with the remaining 40% influenced by factors beyond the scope of the model. Furthermore, Figure 2 presents the PLS–SEM results for the path coefficient values of the structural model, *p*-values, and R-squared determinant coefficient values.

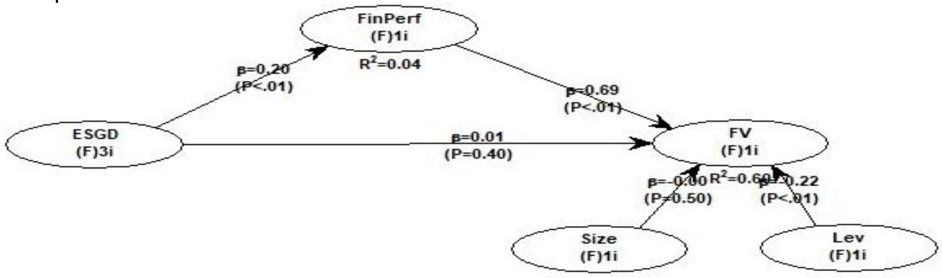


Figure 2. Model Estimation

Source: WarpPLS 8.0 output, 2024

Based on Figure 2, the structural equations produced in this research can be presented as follows:

Fin. Perf = 0.20ESGD + $e_1$........................................................................................ …….. (1)

$FV_{it+1}$ = 0.01ESGD + 0.69Fin. Perf + 0.06Size - 0.22Lev + $e_2$.................................... (2)

Furthermore, Table 6 presents the structural model hypothesis testing results for both direct and indirect effects.

Table 6 Results of Direct Effect Hypothesis Testing

| Structural/Hypothesis | Coefficient Value | *p*-Value | Standard Error | Result |
|---|---|---|---|---|
| ESGD → Fin. Perf | 0.203 | < 0.001 | 0.051 | Significant |
| ESG → Firm value | 0.013 | 0.404 | 0.053 | Not Significant |
| Fin. Perf → Firm value | 0.692 | < 0.001 | 0.048 | Significant |

Source: WarpPLS 8.0 output, 2024

Based on the tables presenting path coefficients and *p*-values, it can be concluded that ESG disclosure had no impact on firm value, but it had a positive and statistically significant effect on financial performance. Furthermore, SEM–PLS analysis results reveal the indirect effect of financial performance on the link between ESG disclosure and firm value. These results are presented in Table 7.

Tabel 7. Indirect Effect

| Indirect effect | Coefficient Value | *p*-Value | Standard Errors | Results |
|---|---|---|---|---|
| ESGD → Fin. Perf → Firm Value | 0.140 | *** 0.001 | 0.037 | Accepted |

Source: WarpPLS 8.0 output, 2024

Based on Table 7, it was found that financial performance played a fully mediating role in the relationship between ESG disclosure and firm value. According to Zhao et al. (2010), if the direct relationship between two variables is insignificant but the indirect effect is significant, then it is categorized as of the indirect-only mediation (full mediation) type.

Research results have shown that firm value was not affected by ESG disclosure. This finding is supported by a coefficient of 0.01 and a *p*-value of 0.40. The resulting *p*-value exceeded the significance limit that was set at 5%. Therefore, the hypothesis stating that there is a positive relationship between ESG disclosure and firm value was not supported. The results of this study indicate that although ESG disclosure played a crucial role within the sustainability framework, it has yet to be directly recognized by investors and other stakeholders in the form of increased firm market value. The low and statistically insignificant coefficient suggests that the market did not perceive ESG disclosure as a primary determinant of firm value, particularly in the short term. A plausible explanation for this finding is that investors and stakeholders tended to respond to ESG information indirectly. Rather than immediately associating ESG disclosure with enhanced firm value, they first evaluated its impact on financial performance. Key aspects such as profitability, operational efficiency, and long-term financial stability are typically assessed as preliminary indicators before ESG effects are reflected in market valuation. In this regard, the influence of ESG on firm value appeared to be mediated rather than direct.

These findings imply that ESG disclosure is yet to be perceived as a sufficiently strong signal in economic decision-making processes, unless it is accompanied by concrete evidence of improved financial performance. Accordingly, companies should prioritize not only the formal aspects of ESG reporting, but also the effective implementation of sustainability practices that demonstrably contribute to economic value creation. From a theoretical perspective, these results reinforce the need to revisit legitimacy theory and signaling theory in the ESG context, particularly within emerging market settings. In many instances, the signals conveyed through ESG disclosure are insufficient to instill investor confidence unless they are supported by robust financial outcomes. This interpretation is consistent with prior studies emphasizing the mediating role of financial performance in the relationship between ESG disclosure and firm value. The results of this research are in line with several previous studies, such as those by Atan (2017), Haryono & Iskandar (2015), and Rohendi et al. (2024), which revealed that ESG disclosure, regardless of its effectiveness, does not lead to significant changes in firm value. In conclusion, the effectiveness of ESG disclosure as a mechanism for enhancing firm value is heavily contingent upon market perceptions of the economic relevance of the disclosed information. This study contributes to the ESG literature by underscoring the importance of understanding the indirect pathways through which ESG disclosure impacts firm value and by encouraging further investigation into potential mediating variables that may strengthen this relationship.

As demonstrated in Table 4, there was a positive and statistically significant relationship between ESG disclosure and financial performance, evidenced by a coefficient of 0.20 and a *p*-value of 0.01. This supports the second hypothesis, which predicts a positive link between ESG disclosure and financial performance. These results are in alignment with stakeholder theory, which suggests that companies engage in environmental and social responsibilities to align with stakeholder expectations, leading to better financial outcomes. ESG initiatives reflect a company's commitment to its stakeholders and contribute to creating a favorable image (Rabaya & Saleh, 2021).

The results of this research are in line with previous research, such as research by Shakil et al. (2019), which found that ESG disclosure contributes to improved financial performance as it receives positive market appreciation. It is also supported by Porter et al. (2019). Likewise, according to Masliza et al. (2021, 2023), ESG disclosure by a company indicates that the company has carried out ESG-related activities, and this will have an impact on financial performance due to the formation of proactiveness on the part of stakeholders. In addition, with some companies disclosing ESG better than others, the information asymmetry between the companies and investors is reduced (Ahmad et al., 2021).

The analysis of the relationship between financial performance and firm value provides empirical support for the hypothesis stating that improved financial performance positively influences firm value. This is evidenced by a coefficient of 0.69 and a *p*-value of 0.01, signifying a statistically significant positive correlation. The results imply that companies demonstrating robust financial performance are more likely to be valued higher in the market. This interpretation is reinforced by descriptive statistics, which indicate that firms with above-average financial outcomes generally attained superior firm value relative to other market players.

The findings of this study reinforce signaling theory, which posits that strong financial performance serves as a positive signal to investors, fostering confidence and encouraging continued investment, thereby increasing firm value. As emphasized by Standfield (2005), a high level of profitability reflects effective resource utilization, income generation, and sound asset management, all of which contribute to a favorable corporate image and the perception of future value potential. This study provides additional empirical evidence supporting the positive relationship between financial performance and firm value, in line with previous studies by Gharaibeh (2018), Hasanudin et al. (2020), and Yanto (2018), which collectively regard financial performance as a key indicator of future growth prospects.

The rationale for this mediating relationship lies in the fact that ESG disclosure reflects a company's commitment to implementing environmental, social, and governance initiatives. When a company actively engages in ESG practices, it signals care for environmental and societal issues and demonstrates sound corporate governance. Such efforts indicate that the firm respects and safeguards stakeholder interests, fostering trust, loyalty, and engagement. This favorable stakeholder perception can lead to increased support, customer satisfaction, and operational efficiencies, all of which enhance financial performance.

Subsequently, strong financial performance becomes a strategic asset, reinforcing the company's positive image and strengthening the signal sent to the market. Investors and stakeholders, recognizing the firm's sustainable and profitable operations, are more likely to invest or support the company in line with their roles, ultimately contributing to higher firm value. Therefore, ESG disclosure, when backed by solid financial performance, becomes a credible and influential signal that drives long-term value creation.

## CONCLUSION

This study investigated the influence of ESG disclosure on firm value in Indonesian companies during the period 2015–2022. The findings reveal that ESG disclosure does not have a direct and significant impact on firm value, thereby contradicting the initial hypothesis stating that such disclosure positively signals value to investors. This result may reflect the current stage of ESG integration in Indonesia, where investors may not yet fully incorporate ESG factors into their valuation decisions. In contrast, ESG disclosure exhibits a significant positive effect on financial performance. Financial performance, in turn, was found to significantly enhance firm value and act as a mediating variable in the relationship between ESG disclosure and firm value. These findings suggest that ESG implementation can enhance internal efficiency, build stakeholder trust, and improve overall business operations, which ultimately leads to stronger financial outcomes and increased firm value. The implications of these findings suggest that ESG initiatives should be viewed not merely as compliance measures but also as strategic tools to improve financial performance and indirectly to strengthen firm value.

This research has limitations in that it was only carried out on companies in one country, namely, Indonesia. Therefore, future studies can examine the impact of ESG disclosure on firm value in companies in a wider area, such as the Asian region or even the whole world, which most likely has differences in social policies, culture, government politics, and geographic location. Apart from that, future researchers can also add other variables that are likely to affect companies in disclosing ESG information, such as CEO power or company characteristics. This study has three contributions. First, it is able to provide an answer to previous studies showing inconsistent directions. Second, it adds to the existing literature by demonstrating that financial performance serves as a mediator in the relationship between ESG disclosure and firm value. Third, it provides an understanding to company managers that ESG disclosure is important to improving financial performance.

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