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The Effectuation of Environmental, Social, and Governance on the Companies' Value in Indonesia

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ABSTRACT: This research to examined the effect of environmental, social and governance (ESG) disclosure on company value. The sample used is companies listed on the Stock Exchange Indonesia (IDX) and own sustainability report period 2020 -2022 as many as 45 companies. This research used regression analysis. . The research results showed that environmental and social disclosure had a positive and significant effect on company value. Meanwhile, governance disclosure had a negative and significant effect on company value.

KEYWORDS: Environmental, Social, Governance, Value, BEI

INTRODUCTION

The world economy is interconnected through trade and investment, so the issue of what reporting companies must disclose to stakeholders has become an important matter (Buallay, 2019). In its development, disclosure regarding financial reports is now felt to be insufficient to meet the needs of company stakeholders regarding information, this has become a concern for company management as a form of concern and service to stakeholders. A successful stakeholder management strategy should lead to better environmental performance, social performance along with governance performance and may also be linked to future financial performance (Velte, 2017).

In recent years ESG scores have become a new trend for investors in determining their investment decisions. Even though this problem emerged a decade ago, until 2016, the Indonesian Stock Exchange (BEI) had not offered written guidelines for ESG reporting, ESG-related training, and had not required ESG reporting as one of the rules for companies to be listed on the stock exchange. However, things are different with the United Nations Sustainability Exchange which expects all companies registered there to disclose the impact of environmental, social and governance practices by the end of 2030 (Sustainability Stock Exchange, 2015).

Disclosure of sustainability reports is growing almost all over the world and continues to increase in number. *Environmental, Social, and Governance* (ESG) is a term generally used in a company's *Corporate Social Responsibility (CSR) which is disclosed in its sustainability report.* ESG disclosure is tasked with assessing practices from the indicators it contains, including environmental (E), social (S) and corporate governance (G).

Disclosure of environmental, social and corporate governance responsibilities is expected to create a good reputation for the company. Increasing company revenue is ultimately based on the increasing level of reputation and consumer trust in the company, which has an impact on gaining loyalty to the company itself. (EY, 2013). Companies that disclose ESG well will be more attractive to financial investors and other stakeholders, and will be financially profitable in the long term due to improved relationships between the company and various parties (Li et al., 2018) .

In Indonesia, developments in the application of ESG aspects for companies also continue to increase. This can be seen by the increasing development of sustainability investment which considers good ESG aspects important. Companies with good ESG implementation will have keen knowledge of long-term strategic issues so they can manage their long-term goals. Companies in Indonesia that are listed on the stock exchange and implement ESG continue to experience an increase in massive exploitation of resources for large financial profits causing enormous environmental damage. (Syafrullah & Muharam, 2017). Therefore, there is support for policies and regulations that are starting to require all institutions, both financial and non-financial services and companies, to practice *sustainability reporting* or *economic sustainability.* Companies are required to be able to disclose more transparent and *valuable information.* For this reason, CSR (Corporate *Social Responsibility)* disclosure carried out by the company in addition to the company's management system (*Good Corporate Governance*) is an important factor for the company's success. It cannot only be seen from the financial aspect that investors pay attention to, ESG also has long-term potential and impacts that can be provided in investments not only limited to shareholders, but also to stakeholders (Almeyda & Darmansyah, 2019). However, a company's ability to deal with current developments is not enough just to use CSR disclosures. For this reason, ESG performance is used as a benchmark for sustainable development in business decisions (Almeyda & Darmansyah, 2019). Of course, ESG disclosure is something that can be used as a benchmark for a company's success as a condition for fulfilling the company's *social* and *environmental* responsibility obligations. the.

The basis for choosing a research theme is that we want to test the effect of implementing *Environmental Social Governance* (ESG) in companies registered in IDX ESG *Leaders* on each company's values. There are several companies whose shares have been selected as IDX ESG *Leaders* as samples in this research. The proxy used to describe company value is Tobin *'s Q*. By having an understanding of the positive impacts obtained from *environmental applications Social Governance* hopes that all business actors in Indonesia can take more initiative to participate and actively support sustainable development through improving ESG-based performance. As explained by (Xie et al., 2019), the increasing awareness of companies to implement sustainability strategies and disclose environmental, social and governance (ESG) information has had the impact of fundamental changes in management and business models.

THEORETICAL REVIEW

Environmental, Social, and Governance

Over the last two decades, disclosure of sustainability reports has developed greatly throughout the world and continues to increase in number. *Environmental, Social, and Governance* (ESG) is a term generally used in a company's *Corporate Social Responsibility (CSR) which is disclosed in its sustainability report.* ESG has been in the limelight lately. Apart from the financial aspects that investors pay attention to, ESG also has long-term potential and impacts that can be provided in investments not only limited to shareholders, but also to stakeholders (Almeyda & Darmansyah, 2019). Companies with good ESG implementation will have keen knowledge of long-term strategic issues so they can manage their long-term goals. ESG information can direct analytical forecasts to be more targeted and realistic. Company management also has the possibility of more precise information to be handled and results that can exceed its target market (Tarmuji, Maelah, & Tarmuji, 2016). The development of increasingly large companies means that conflicts can occur more frequently between principals and agents due to differences in their respective mindsets and prominent interests. Company owners certainly sometimes have different thoughts from managers (Jensen & Meckling, 1976). Shareholders pay more attention to the sustainability of a company which can be proven by ESG in *the sustainability report* (Connelly, 2011). The right solution to reduce conflict in this agency is to have managerial ownership in *good corporate governance* . With managerial ownership, management who own shares can act as shareholders and participate in decision making within the company. It is also stated that shareholders pay more attention to the sustainability of a company which can be proven by ESG in *the sustainability report* (Connelly, 2011).

There is a theory where there is a perspective from shareholders regarding the company's ability to obtain more company value in the future. Company management is responsible for this information to shareholders (Spence, 1973). The company's financial reports are very important and serve as a guide for shareholders. It can also be used as a core ingredient in considering and making investment decisions. Better information about the company can encourage shareholders to communicate this information to potential investors so that the company's share price can rise (Moeljadi & Supriyati, 2014). The information received by shareholders is not only about financial performance as represented by company profits, but nowadays it has also been proven that company *sustainability information* can influence long-term investment decisions of shareholders (Moratis, 2018).

The Influence of ESG on Company Value

In neoclassical theory, it is stated that the relationship between ESG and economic outcomes is consistently negative. The issue of ESG variables that have an impact on company performance, especially financial, is a very controversial topic (Vance, 1975). As time goes by, ESG is starting to be noticed by decision makers who pay attention to corporate ethics and social accountability, especially in environmental management (Lamond, 2007). In the relationship between investment financial performance and environmental management, companies generally believe that cost savings in environmental programs can provide advantages or achieve greater customer satisfaction. On the other hand, if a company invests in poor environmental management either due to inefficiency or unnecessary investment, the company's performance will be impacted the negative.

Sustainable development activities are expected to encourage greater demand for products and services from companies which will increase company growth and reduce business risks (Buallay, 2019). When demand for a company's products and services increases, the company's production also increases. This increase in production has an impact on the company, namely increasing the costs that must be incurred by the company. However, ESG has a quite positive impact on companies. By disclosing sustainability reports containing both financial and non-financial information, information regarding company performance can be provided and accounted for to shareholders in order to satisfy shareholder demands. ESG disclosure that has a positive response from the public can increase the capital investment that can be obtained. This also means that the company can use the additional capital to further increase production, increase sales, and also increase the company's profitability (Safriani & Utomo, 2020).

The relationship that this research wants to reveal is that the implementation of ESG has a positive effect on company value, so that a high ESG score will result in high company performance. Empirical findings conducted by (Buallay, 2019), (Safriani & Utomo, 2020), (Fatemi, Glaum, & Kaiser, 2018), and (Shakil, Mahmood, Tasnia, & Munim, 2019) support that ESG has a positive effect on value company. So the hypothesis that can be drawn is: following:

H1: ESG has a positive effect on company value.

RESEARCH METHOD

This research uses companies that are listed on the Indonesia Stock Exchange (BEI) and have sustainability reports from 2018-2020. This research collects data using several criteria: Companies that are listed on the Indonesia Stock Exchange (BEI) or that have a *sustainability report* in 20 20 -202 2 , Companies that have not experienced delisting in 20 20 - 202 2 , Companies that have complete financial reports. Financial ratio information is taken from company financial reports and IDN Financials. Meanwhile, for ESG information *Score* is taken from the BGK ESG *Index* . This research was conducted using classical assumption test analysis and using the SPSS measuring tool. The tests that will be carried out are the normality test, multicollinearity test, heteroscedasticity test, and test autocorrelation.

RESULTS & DISCUSSION

The number of company samples for this research was 45 companies with total observations of 135 companies. Descriptive statistics as seen from Table 3. of each variable show that the ESG variable has an average value of 0.247 (24.7%) so it can be said that ESG *disclosure* in the companies in Indonesia studied is currently still low because it is still below 50 percent (Alfaruq, 2021). The PBV variable has an average value of 1.225, meaning that companies that have ESG *disclosure* and are currently being researched have a high market value because they have a PBV value above 1.

The total assets variable has an average value of 155,746,297.16 rupiah and tends to experience total asset growth of 13.85%, which means that companies that have ESG *disclosure* and are currently being researched have large assets and tend to experience positive growth over three years. (2018 – 2020). The company age variable has an average value of 19.47 years, which means that companies that have ESG *disclosure* and are currently being researched have had a long operational period so they have extensive experience. Good.

Regarding the industrial sector variable, the majority of companies that have *sustainability reports* come from the non-financial sector, namely 30 companies, while the financial sector is 15 companies, meaning that there are still many companies from the non-financial sector that have not implemented ESG *disclosure* considering the proportion of companies listed on the IDX. the majority come from the non-financial sector. The DAR variable has an average value of 0.610, meaning that the majority of companies that carry out ESG *disclosure* , most of their company assets are the result of debt financing (more than 50%). The *sales growth* variable has an average value of 0.124 (or 12.4%) meaning that the majority of companies that carry out ESG *disclosure* mostly have positive sales growth during the three years of research (2018 -2020).

Table 3. Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Std. Deviation
PBV	135	0.210	4.61	1,225	0.779
ROE	135	-0.233	0.925	0.091	0.110
ESG	135	0.023	0.863	0.247	0.177
LNTA	135	13,254	21,137	17,727	1,603
Age	135	4	38	19,470	8,816
IND	135	0	1	0.333	0.473
DAR	135	0.109	0.890	0.610	0.230
S.G	135	-0.896	9,235	0.124	0.841

This research bases its data analysis technique on *Ordinary Least Square regression* , therefore the classical assumption test needs to be carried out in an effort to fulfill the assumption that there is a linear relationship between variables. The classical assumption test was carried out on empirical model 1 and empirical model 2 in the form of a normality test using Kolmogorov Smirnov. The results show that the data is normally distributed in both empirical models. The multicollinearity test was carried out using *tolerance* and VIF values. The results show that all independent and control variables are free from symptoms of multicollinearity in both models. The heteroscedasticity test was carried out using the Glejser test where empirical models 1 and 2 did not experience symptoms of heteroscedasticity. The autocorrelation test was carried out using *a runs test* , showing that there were no symptoms of autocorrelation in empirical models 1 and 2.

The results of the classical assumption test state that empirical model 1 and empirical model 2 fulfill the assumption that there is a linear relationship between variables so that it can be continued for further statistical tests. The following are the results of statistical tests to prove the hypothesis for empirical model 1 and empirical model 2:

Table 4. Effect of ESG on Company Value

	ROE		**PBV**	
Variable	Coef. regression	ρ *value*	Coef. regression	ρ *value*
ESG	-0.111	0.039	-0.282	0.438
LNTA	-0.005	0.554	0.190	0.001
LNAGE	-0.036	0.070	-0.015	0.912
IND	0.095	0.002	0.261	0.193
DAR	-0.170	0.006	-1,875	0,000
S.G	0.004	0.719	-0.123	0.103
Date Obsv.	135		135	
Adj. R2	0.083		0.157	
F *statistic (p-value)*	3,021 (0.009)		5,165 (0.000)	

Based on Table 4, it can be seen that empirical model 1 ESG variables have a negative and significant effect on ROE. Simultaneously, the F test shows that the ESG variables and control variables (LNTA, LNAGE, IND, DAR and SG) have a significant effect. For the control variables in empirical model 1, only the industrial sector variable (IND) has a significant positive effect and *financial leverage* (DAR) has a negative effect. significant.

Empirical model 2 shows that ESG variables do not have a significant and negative effect on PBV. Simultaneously, the F test shows that the ESG variables and control variables (LNTA, LNAGE, IND, DAR and SG) have a significant effect. For the control variables in empirical model 2, only the *firm size variable* (LNTA) has a significant positive effect and *financial leverage* (DAR) has a negative effect. significant.

Sustainable development and sustainability reporting *have* been considered important aspects of a country's economic development. This is proven by the increasing number of studies on the impact of ESG performance on other aspects, especially on how it influences company performance (*firm value*) with the aim of encouraging companies around the world to start complying with sustainability reporting (Junius et.al., 2020). This research aims to prove the positive influence of ESG performance on *firms value* .

Research on ESG performance is usually carried out in developed countries, so further research is needed on ESG performance in developing countries (Tarmuji, Maelah, & Tarmuji, 2016). The research was conducted on Malaysia, Indonesia, Singapore and Thailand to see whether there were differences in ESG performance if the research was conducted in developing countries. In addition, the selection of developing countries is expected to expand the scope of the literature.

The results of this research show that empirical model 1 ESG variables have a significant effect on ROE but are negative, meaning the hypothesis is rejected. Empirical model 2 also shows similar results that ESG variables do not have a significant and negative effect on PBV. These results are in line with research conducted (Junius, Adisurjo, Rijanto, & Adelina, 2020); (Ahmed, 2021); and (Ramasamy, Ting, & Yeung, 2007) who tried to see the positive influence of ESG performance on *firm value* (company performance). Empirical findings from various studies show that there is no relevance in assessing ESG performance towards firm value (company performance) in the context of implementing sustainability reporting *in developing* countries. *countries*).

The measurement of the average ESG performance value of Indonesian companies included in this research can still be said to be low, namely 24.7%. These results can strengthen evidence that the implementation of *sustainability reporting* in Indonesia is still weak. In addition, only 98 of 713 (or around 13.74%) companies listed on the IDX made *sustainability reporting* in 2020. Furthermore, the results of this research show that information about ESG *Score* or sustainable development activities carried out by companies in Indonesia was unable to increase (empirical model 2), more contradictory it actually reduced the company's market value (empirical model 1).

This is thought to occur because consumers, employees and other stakeholders do not yet see the added value of corporate social responsibility activities that are realized through the implementation of *sustainability reporting* . Research by Chou & Chen (2004) states that for Asian countries, most consumers are sensitive to price, not to issues of sustainable development or corporate social responsibility. In a survey of consumer purchasing behavior in Malaysia, Ahmed (2003) found that 85% of respondents considered the price and quality of a product to be important influencing factors that influence the decision to purchase a product. Only 3% consider a company's CSR activities to be an important factor in purchasing decisions they.

These results may imply that consumers in developing countries like Indonesia may not appreciate corporate social responsibility and are unwilling to pay a premium or even pledge allegiance to a product or service because of the nature of the corporate social responsibility they undertake (actively making sustainability reporting *)* . In other words, the marginal income obtained by companies that actively make *sustainability reporting* is not large (Ramasamy, Ting, & Yeung, 2007). Whether or not a company is able to increase profits by being active in making *sustainability reporting* will depend on the marginal costs of CSR activities, which can actually reduce the company's profitability (empirical model 1).

CONCLUSION

Based on the results of the analysis that has been carried out, it shows that: ESG performance has a negative and significant effect on ROE in empirical model 1. Simultaneously, it shows that the ESG variables and control variables (LNTA, LNAGE, IND, DAR and SG) have a significant effect. Regarding the control variables in empirical model 1, industrial sector (IND) has a significant positive effect and *financial leverage* (DAR) has a significant negative effect, while *firm size* , *firm age* and *sales growth* have no significant effect.

ESG performance has no significant and negative effect on PBV in empirical model 2. Simultaneously, it shows that the ESG variables and control variables (LNTA, LNAGE, IND, DAR and SG) have a significant effect. Regarding the control variables in empirical model 2, *firm size* (LNTA) has a significant positive effect and *financial leverage* (DAR) has a significant negative effect, while industrial sector, *firm age* and *sales growth* have no significant effect. Companies need to improve ESG performance due to the low ESG value during this research period. Increasing ESG performance is expected to improve other aspects, including Performance Company.

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