How to Cite
Ariani, N. P., Sisdyani, E. A., Yasa, G. W., & Ratnadi, N. M. D. (2025). Assessing the impact of Environmental, Social, and Governance (ESG) performance on corporate profitability: The moderating role of firm size. *International Journal of Business, Economics and Management*, *8*(2), 99-107.
https://doi.org/10.21744/ijbem.v8n2.2398

Assessing the impact of Environmental, Social, and Governance (ESG) performance on corporate profitability: The moderating role of firm size

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Abstract---*This study aims to empirically test the extent to which environmental performance, social performance, and governance performance can affect company profitability and empirically test the ability of company size to moderate the influence of environmental performance, social performance, and governance performance on company profitability. This study was conducted on non-financial companies listed on the Indonesian Stock Exchange. The independent variables in this study are environmental performance, social performance, and governance performance, where data were obtained from Refinitiv Eikon. The dependent variable in this study is company profitability. The moderating variable in this study is company size. The sampling technique used was a purposive sampling technique, and a sample of 61 companies, or 294 total observations. The data analysis technique was carried out using Moderated Regression Analysis. The results of the analysis empirically show that environmental performance, social performance, and governance performance have a positive effect on profitability. Company size is able to moderate the positive effect of environmental performance. Company size cannot moderate the effect of social performance and governance performance on profitability. This study can help companies understand the importance of integrating ESG risks into planning and decision-making. In addition, regulators such as the Financial Services Authority (OJK) can play an important role in encouraging ESG reporting across all types and sizes of companies.*
Keywords---*Environmental Performance, Firm Size, Governance Performance, Profitability, Social Performance.*

Introduction

Profitability is a key indicator of a company's financial health and long-term sustainability, reflecting its ability to generate profits through effective resource management and cost control (Pangentas & Prasetyo, 2023; Priandhana, 2022). Companies with stable and sustainable profitability tend to have stronger positions in the market, greater investor appeal, and the capacity to drive economic expansion (Brulhart et al., 2019).

In Indonesia, where 63.96% of GDP is supported by real sectors such as manufacturing, trade, agriculture, construction, and transportation (Bank Indonesia, 2023), the profitability of non-financial companies plays a crucial

ISSN 2632-9476
Submitted: 27 April 2025 |Revised: 09 May 2025 | Accepted: 18 June 2025

role in fostering macroeconomic stability and national productivity. However, assessments of corporate performance are no longer solely reliant on financial indicators. Regulatory frameworks, such as Indonesia's Financial Services Authority Regulation No. 51/POJK.03/2017, mandate the adoption of sustainable finance principles, requiring public companies to integrate environmental, social, and governance (ESG) factors into their business strategies and disclosures (Rahmaniati & Ekawati, 2024).

ESG performance has emerged as a global standard for evaluating corporate sustainability, with increasing attention from investors, creditors, and analysts (Sustainable Growth, 2023). Environmental performance reflects a company's capability to minimize ecological impact and improve operational efficiency (Naeem & Çankaya, 2022). Social performance relates to how companies build meaningful stakeholder relationships and contribute to community welfare, which can enhance brand loyalty and employee retention (Kartana et al., 2024). Governance performance ensures decision-making transparency and risk mitigation, supporting profitability through lower capital costs and improved trust (Ticoalu et al., 2021).

Data from Revinitiv Eikon (2024) on Indonesian public companies operating in strategic sectors—such as mining and infrastructure—show a positive trend in ESG scores between 2021 and 2023. This indicates a growing corporate commitment to balancing financial goals with social and environmental responsibilities. Moreover, firm size may influence the quality and scope of ESG disclosures. Larger firms generally have better resources to implement structured ESG reporting and may gain greater reputational and financial returns (Nuryaningrum & Andhaniwati, 2021; Prayogo et al., 2023). Large firms also have more resources to increase company value because they have better access to external information sources than small companies (Abdi et al., 2022).

Despite the increasing relevance of ESG, empirical evidence on its impact on profitability remains inconclusive. Some studies report a positive relationship (Ali et al., 2025; Naeem & Çankaya, 2022), while others identify negative or insignificant effects (Cantero-Saiz et al., 2025; Duque-Grisales & Aguilera-Caracuel, 2021; Menicucci & Paolucci, 2023; Wu & Li, 2025). These inconsistencies highlight the need for further investigation.

Previous studies have produced inconsistent results regarding the impact of environmental, social, and governance performance on corporate profitability, with some reporting positive effects while others identifying negative or insignificant relationships. This study aims to examine the effect of ESG performance—specifically environmental, social, and governance dimensions—on corporate profitability, while also considering firm size as a moderating variable. The inclusion of firm size provides deeper insights into how the scale of operations may shape the effectiveness of ESG practices in enhancing profitability (Candio, 2024; Fdez-Galiano & Feria-Dominguez, 2024; Mandas et al., 2024).

Literature Review and Hypothesis Development

Environmental Performance and Corporate Profitability

According to stakeholder theory (Freeman, 1984), companies have responsibilities beyond shareholders, including the natural environment. Environmental performance refers to how well a firm manages its environmental impact through sustainable resource use, emission control, and waste management. Prior studies (Pangentas & Prasetyo, 2023; Aditama, 2022; Chininga et al., 2023) show that high environmental performance improves reputation, mitigates regulatory risk, and attracts environmentally conscious investors and customers. This ultimately enhances profitability.

H1: Environmental performance has a positive effect on corporate profitability.

Social Performance and Corporate Profitability

Stakeholder theory emphasizes the importance of maintaining strong relationships with employees, customers, and communities (Freeman, 1984). Social performance involves corporate initiatives aimed at contributing to societal welfare. Firms with strong social performance tend to gain trust, reduce employee turnover, and enhance customer loyalty, which supports financial gains (Kartana et al., 2024; Bischoff et al., 2024).

H2: Social performance has a positive effect on corporate profitability.

Governance Performance and Corporate Profitability

Governance performance reflects a company's commitment to transparency, accountability, and strong internal controls. Effective governance minimizes operational risk and improves strategic decision-making, which can lead to improved asset utilization and long-term profitability (Astaningrum & Widodo, 2023; Ticoalu et al., 2021).

H3: Governance performance has a positive effect on corporate profitability.

Firm Size to Environmental Performance

Larger firms have more resources to adopt advanced environmental management systems and sustainable technologies (Nuryaningrum & Andhaniwati, 2021). Stakeholder pressure is also more intense for large firms, pushing them toward better environmental compliance, which may enhance profitability.

H4: Firm size positively moderates the relationship between environmental performance and corporate profitability.

Firm Size to Social Performance

Large firms can invest more in social initiatives and develop dedicated teams to manage stakeholder relations. This allows them to convert social efforts into competitive advantages more effectively (Safriani & Utomo, 2020; Ho et al., 2019).

H5: Firm size positively moderates the relationship between social performance and corporate profitability.

Firm Size to Governance Performance

Large firms typically have more complex and robust governance structures, including better compliance systems and greater investor transparency. These attributes increase investor confidence and reduce capital costs, thereby strengthening the governance–profitability link (Aditama, 2022; Fu & Li, 2023).

H6: Firm size positively moderates the relationship between governance performance and corporate profitability.

Methods

This study focuses on publicly listed companies on the Indonesia Stock Exchange (IDX) during the period 2017–2023. The starting year of 2017 is significant due to the issuance of the Indonesia Financial Services Authority (OJK) Regulation No. 51/POJK.03/2017 concerning the implementation of sustainable finance for financial institutions, issuers, and public companies, which mandates the disclosure of sustainability reports. The research specifically targets non-financial firms**,** as these companies are more representative of real-sector economic activity. Firms in the real sector—particularly in manufacturing and extractive industries—tend to have more measurable and direct environmental impacts, making their ESG disclosures highly relevant (Rahmawaty & Harahap, 2024). Moreover, ESG disclosure is crucial for communicating a company's understanding of material sustainability issues that matter to stakeholders. Such disclosures enable investors to assess key risks and opportunities associated with long-term investment decisions.

The population in this study consists of companies listed on the Indonesia Stock Exchange (IDX). This study focuses on a sample of non-financial companies listed on the IDX. Non-financial firms are chosen to better reflect real sector economic activity. Companies operating in the real sector—particularly in manufacturing and extractive industries—tend to have more direct and measurable environmental impacts, making ESG disclosure particularly relevant (Rahmawaty & Harahap, 2024; Lina et al., 2024). The sampling technique used is non-probability sampling with a purposive sampling approach. Companies are selected based on specific criteria: (1) availability of financial data and (2) availability of ESG scores for the period 2017 to 2023.

MRA is used to test whether the strength or direction of the relationship between independent variables and the dependent variable is influenced by a moderating variable. In this context, firm size is expected to either strengthen or weaken the effect of ESG performance on profitability, providing insights into the conditional nature of these relationships (Zahid et al., 2022; Ramírez-Orellana et al., 2023).

Result and Discussion

Normality Testing

The normality test is conducted to determine whether the residuals of the regression model are normally distributed. A good regression model is characterized by residuals that are normally or approximately normally distributed. If the residuals are not normally distributed, the model's predictions may be biased and unreliable. In this study, the normality test is carried out using the Kolmogorov–Smirnov (K–S) test**.** The results of the normality test are presented in Table 1.

Table 1
Normality Test Result

	Unstandardized Residual
N	294
Asymp. Sig. (2-tailed)	0,200

Secondary Data, 2024

Based on the test results presented in Table 1, it shows that the Asymp. Sig. (2-tailed) The value is 0.200. This value is greater than the significance level of 0.05. Therefore, it can be concluded that the data is normally distributed, so the model is suitable for further analysis.

Multicollinearity Test

The multicollinearity test aims to determine whether there is a correlation among the independent variables in the regression model. A good regression model should not exhibit correlation among the independent variables or be free from multicollinearity. If a regression model containing multicollinearity symptoms is forced to be used, it will produce biased prediction results. To detect the presence or absence of correlation among independent variables, the tolerance value and variance inflation factor (VIF) can be examined. If the tolerance value is more than 10 percent or the VIF is less than 10, then there is no multicollinearity (Utama, 2016). The results of the multicollinearity test in this study are shown in Table 2.

Table 2
Multicollinearity Test Results

	Tolerance	VIF
ENV	0,448	2,230
SOC	0,397	2,521
GOV	0,673	1,485
SIZE	0,595	1,680

Secondary Data, 2024

Based on the results presented in Table 2, the tolerance values are greater than 0.10 and the variance inflation factors (VIF) are less than 10. These findings indicate that there is no multicollinearity present in the regression model, suggesting that the model is appropriate for making predictions.

Heteroskedasticity Test

The heteroskedasticity test is conducted to determine whether the variance of the residuals remains consistent across all observations. A good regression model is characterized by homoscedasticity, or equal variance in the residuals. If heteroskedasticity is present, it can lead to biased or inefficient parameter estimates (Utama, 2016). In this study, the Glejser test is used to assess the presence of heteroskedasticity. The results of this test are shown in Table 3.

Table 3
Heteroskedasticity Test Result

	B	Std. Error	Beta	t	Sig.
Konstanta	0,170	0,477		1,633	0,104
ENV	0,022	0,011	0,094	1,117	0,265
SOC	0,116	0,061	0,170	1,897	0,059
GOV	0,319	0,507	0,095	1,377	0,170
SIZE	0,435	0,405	0,071	1,076	0,283

Secondary Data, 2024

Based on the results in Table 3, the significance value (Sig.) is greater than 0.05, indicating that there is no evidence of heteroskedasticity in the regression model. Therefore, the model is considered homoscedastic and appropriate for prediction purposes.

Autocorrelation Test

To detect the presence of autocorrelation, or the influence of previous observations on current ones in a regression model, an autocorrelation test is conducted. If autocorrelation exists in a model, the resulting predictions may be biased or unreliable (Utama, 2016). In this study, the Durbin-Watson (DW) test is used to identify the presence of autocorrelation. The results of the autocorrelation test are presented in Table 4.

Table 4
Autocorrelation Test

R	R Square	Adjusted R Square	Durbin-Watson
0,40	0,16	0,15	1,95

Secondary Data, 2024

Based on the results in Table 4, the Durbin-Watson (DW) statistic is 1.95, which falls within the acceptable range of $1.82 < 1.95 < 2.17$. This indicates that the regression model does not exhibit autocorrelation and is therefore considered suitable for predictive analysis.

Moderated Regression Analysis

A regression model that incorporates interaction terms among variables is known as Moderated Regression Analysis (MRA)**.** MRA is used to examine the relationship between independent and dependent variables, particularly in the presence of a moderating variable that may either strengthen or weaken the effect of the independent variable on the dependent variable.
The interaction test results from this study are interpreted as follows:

Model Fit Test
The ANOVA (F-test) is used to evaluate the overall significance of the regression model (Utama, 2016). If the significance value is ≤ 0.05**,** it indicates that the independent variables collectively have a significant influence on the dependent variable, and thus the model is deemed appropriate for prediction. The F-test results are shown in Table 5.

Table 5
Model Fit Test Result

	Sum of Squares	df	*Mean Square*	F	Sig.
Regression	8045,982	7	1149,426	11,476	0,000
Residual	28646,467	286	100,162		
Total	36692,449	293			

Secondary Data, 2024

Based on Table 5, the calculated F-value is 11.476 with a significance level of 0.000. Since the significance probability is well below 0.05, it can be concluded that environmental performance**,** social performance**,** governance performance**,** and the moderating variable jointly have a significant effect on corporate profitability. Therefore, the regression model is considered valid for predictive purposes.

Coefficient of Determination (R^2)

The coefficient of determination (R^2) measures the goodness of fit of the regression model, indicating the proportion of variance in the dependent variable that can be explained by the independent variables (Utama, 2016). The R^2 value obtained in this study is presented in Table 6.

Table 6
Coefficient of Determination (R^2)

R	R Square	Adjusted R Square	Std. Error of the Estimate
0,468	0,219	0,200	10,00812

Secondary Data, 2024

Based on Table 6, the R^2 value is 0.219. This indicates that 21.9% of the variation in corporate profitability can be explained by the independent variables: environmental performance, social performance, governance performance, and the moderating variable. The remaining 78.1% is explained by other factors not included in the model. In accounting and finance studies, it is very common to find that profitability is not only influenced by one factor. Even factors such as company reputation, customer satisfaction, and product innovation can have a significant impact on firm profitability.

Test of Individual Significance (t-test)

The t-test is used to assess the statistical significance of individual independent variables in explaining the dependent variable. It evaluates the extent to which each predictor independently contributes to the model. The results of the t-test are presented in Table 7.

Table 7
Moderate Regression Analysis Test Result

	B	Std. Error	Beta	t	Sig.
Konstanta	55,639	6,959		4,211	0,000
ENV	2,485	0,868	5,151	2,863	0,005
SOC	6,559	1,069	11,580	6,137	0,000
GOV	0,302	0,049	11,928	6,193	0,000
SIZE	7,231	1,708	0,686	4,233	0,000
ENV*SIZE	0,119	0,040	5,445	3,007	0,003
SOC*SIZE	-1,145	0,868	-2,334	-1,319	0,188
GOV*SIZE	-0,055	0,040	-2,442	-1,365	0,173

Secondary Data, 2024

Regression Equation and Coefficient Interpretation

Based on Table 7, the regression equation derived from the analysis is as follows:

$$PROFIT = 55.639 + 2.485(ENV) + 6.559(SOC) + 0.302(GOV) + 7.231(SIZE) + 0.119(ENV \times SIZE) - 1.145(SOC \times SIZE) - 0.055(GOV \times SIZE)$$

Interpretation of the coefficients:

1) Intercept ($\alpha = 55.639$): When all independent variables are held at zero, the predicted value of corporate profitability is 55.639.
2) $\beta 1 = 2.485$ (ENV): A one-unit increase in environmental performance increases profitability by 2.485, assuming other variables are constant.
3) $\beta 2 = 6.559$ (SOC): A one-unit increase in social performance increases profitability by 6.559, assuming other variables are constant.
4) $\beta 3 = 0.302$ (GOV): A one-unit increase in governance performance increases profitability by 0.302, assuming other variables are constant.
5) $\beta 4 = 7.231$ (SIZE): A one-unit increase in firm size increases profitability by 7.231, assuming other variables are constant.
6) $\beta 5 = 0.119$ (ENV × SIZE): Each unit increase in firm size strengthens the positive effect of environmental performance on profitability by 0.119, indicating a significant moderation.

7) β6 = -1.145 (SOC × SIZE): Each unit increase in firm size weakens the effect of social performance on profitability by 1.145, indicating a negative but insignificant moderation.
8) β7 = -0.055 (GOV × SIZE): Each unit increase in firm size weakens the effect of governance performance on profitability by 0.055, also an insignificant moderation.

Hypothesis Testing (t-Test Results)

Based on Table 7, the individual significance tests yield the following results:

H1 – Environmental performance significantly affects profitability ($p = 0.005 < 0.05$), supporting the hypothesis that environmental performance positively influences corporate profitability.
H2 – Social performance significantly affects profitability ($p = 0.000 < 0.05$), supporting the hypothesis that social performance positively influences profitability.
H3 – Governance performance significantly affects profitability ($p = 0.000 < 0.05$), supporting the hypothesis that governance performance positively influences profitability.
H4 – Interaction of environmental performance and firm size is significant ($p = 0.003 < 0.05$), indicating that firm size positively moderates the relationship between environmental performance and profitability.
H5 – Interaction of social performance and firm size is not significant ($p = 0.188 > 0.05$), meaning firm size does not moderate the relationship between social performance and profitability.
H6 – Interaction of governance performance and firm size is not significant ($p = 0.173 > 0.05$), indicating that firm size does not moderate the relationship between governance performance and profitability.

Moderation Classification

Given that both firm size and ENV × SIZE are statistically significant, firm size is identified as a quasi-moderator. This means that firm size not only affects profitability directly but also moderates the relationship between environmental performance and profitability.

However, since firm size significantly affects profitability, while SOC × SIZE and GOV × SIZE do not significantly influence profitability, firm size in these two interactions acts as a predictor moderator. In this case, firm size serves only as an independent predictor rather than a true moderator in the relationships involving social and governance performance.

Conclusion

This study investigates the effect of environmental, social, and governance (ESG) performance on corporate profitability, with firm size as a moderating variable, using data from non-financial companies listed on the Indonesia Stock Exchange from 2017 to 2023. The findings confirm that environmental performance, social performance, and governance performance each have a positive and significant impact on profitability, supporting stakeholder theory, which emphasizes the importance of responsible business practices in enhancing firm value.

The interaction analysis reveals that firm size significantly moderates the relationship between environmental performance and profitability. This indicates that larger firms are better positioned to convert environmental initiatives into financial gains due to superior resource availability and stakeholder pressure. However, firm size does not significantly moderate the effects of social and governance performance on profitability, suggesting that these relationships are less influenced by the scale of the firm. In these cases, firm size functions more as an independent predictor than a true moderator.

Empirical And Practical Contributions

This research provides an empirical contribution by providing concrete evidence on the relationship between ESG commitment and corporate profitability by integrating two main theoretical frameworks, namely stakeholder theory and agency theory. Through quantitative data analysis of companies implementing ESG policies, this study evaluates the extent to which ESG performance has a positive impact on profitability, as well as the role of governance mechanisms in strengthening or inhibiting this influence. Thus, this study offers findings that enrich the literature with a holistic approach that bridges principals and agents especially in the context of emerging markets.

This research provides practical contributions by providing data-driven guidance for companies in integrating environmental, social, and governance (ESG) factors into their business strategies and decision-making processes. The research findings can be used to help companies identify critical ESG risk areas, develop internal policies that

are responsive to sustainability issues, and strengthen ESG reporting practices to increase transparency and investor appeal. Furthermore, insights from this research can also be used to shape an organizational culture that is oriented towards sustainability and innovation, which ultimately contributes to increasing competitive advantage and long-term profitability. In addition, the results of this research are useful for regulators such as OJK in designing more inclusive and effective ESG reporting policies, especially in encouraging SME participation in a sustainable and responsible business ecosystem.

Research Limitation

First, the research focuses solely on non-financial companies listed on the Indonesian Stock Exchange, which may restrict the generalizability of the findings to financial institutions or firms operating in different regulatory and economic contexts. Second, the study relies on secondary data obtained from Refinitiv Eikon and company financial reports. The accuracy of the ESG scores and financial metrics depends heavily on the quality and consistency of corporate disclosures, which may vary across firms and years. Third, the use of unbalanced panel data means that not all firms have complete observations for each year in the 2017–2023 period, potentially affecting the robustness of the results. Fourth, this study includes only one moderating variable—firm size—without considering other contextual or structural moderators such as industry type, ownership structure, or market conditions, which could also influence the relationship between ESG performance and profitability. Finally, as the analysis is based on regression models using observational data, causal inferences cannot be firmly established, and potential endogeneity issues, such as reverse causality, may still be present.

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