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The Effect of Sustainability Reports on FirmValue with Institutional Ownership as A Moderating Variable

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Abstract

Purpose: This research wants to enrich research that studies the effect of sustainability reporting on firm value, which is still inconsistent. In addition, this study considers the supervisory mechanism factor in the form of institutional ownership to determine whether the effect of sustainability reporting on firm value is different in companies with high institutional ownership and companies with low institutional ownership.

Method: The study utilised purposive sampling to select companies listed on the Indonesia Stock Exchange (IDX) that consistently published sustainability and financial reports from 2017 to 2020, resulting in a sample of 39 companies. For hypothesis testing, the research employed the STATA 17 software, followed by descriptive analysis, panel data regression analysis, determination of coefficients, and tests for both simultaneous and partial significance.

Result: Sustainability reporting positively influences firm value. Moreover, the study indicates that institutional ownership does not alter the impact of sustainability reports on firm value. Future research should focus on examining companies within similar sectors to yield more reliable results concerning how sustainability reports affect firm value, considering the specific characteristics of companies across different industries.

INTRODUCTION

Management aims to increase shareholder wealth, but recent phenomena such as climate change and social inequality have changed the company's goals to prioritize attention to all stakeholders (Ebaid, 2023). In other words, companies now pay more attention to financial and non-financial performance. Shareholder prosperity is a logical consequence if the company pays attention to the interests of all stakeholders. Companies strive to contribute positively to the environment and social and organizational management with good governance and report to the public to improve their financial performance (Arayssi & Jizi, 2024).

Business development in the era of globalization not only focuses on financial matters or the condition of a company but also pays attention to a combination of economic, social, and environmental aspects. Of the three elements of sustainable development, companies must allocate costs for social responsibility so that firm value increases (Nguyen, 2020). This problem concerns government companies and business people, as they need to find the right solution to overcome increasingly complex environmental damage (Febriyanti, 2021). Therefore, to realize the sustainability of the earth and the continuity of economic development specifically, this is done by formulating the concept of sustainable development within the company (Kurniawan et al., 2018).

Companies must adhere to the globally recognized Global Reporting Initiative (GRI) standards when compiling sustainability reports. According to Zakarias & Bimo (2021), the GRI standard requires disclosure in three main areas: economic (GRI 200), environmental (GRI 300), and social (GRI 400), totaling 89 disclosure items. Kurniawan et al. (2018) note that disclosing economic, social, and environmental details enhances public trust and boosts company value (Godha & Jain, 2015). Sustainability reporting can also improve internal operations and stakeholder relationships, attracting investors and increasing stock value.

Institutional ownership is significant not just in developed economies but also in emerging markets. In countries like the United States and the United Kingdom, over half of the shares are held by institutional investors, giving them a substantial influence over market dynamics (Doğan, 2020). Furthermore, the extent of institutional ownership directly impacts firm value; larger institutional stakes often lead to management being more driven to maximize profits for investors. Institutional owners also enhance governance by closely monitoring management decisions, improving policy-making, and scrutinizing the company's economic performance and sustainability (Febriyanti, 2021).

Company value is a description of the conditions that have been achieved by the company and is in line with the value of public trust; this value can also be interpreted as good or bad managerial control of its finances (Febriyanti, 2021). The calculation of company value uses Tobin's Q because this method uses market prices, which affects the investor's point of view (Kurniawan et al., 2018). Unlike other measurement methods, Tobin's Q is unaffected by managerial manipulation and different accounting methods (Swarnapali, 2020).

This study wants to fill the research gap of previous research in sustainability reporting and firm value. First, the effect of sustainability reporting on firm value still needs to be consistent; some studies find a positive or negative effect, and some find no effect (Tandelilin & Usman, 2023). Second, in contrast, Tandelilin & Usman (2023) also mentioned ownership factors in the form of institutional ownership as a moderating variable.

From the legitimacy theory perspective, pressure is needed on companies with strong social capabilities and relevance to the environment, showing a significant commitment to reporting activities in validating the company to society (Balluchi et al., 2021). The disclosure of environmental and social categories in the company's sustainability report can enhance a positive image and obtain legitimacy from the community and related stakeholders (Kurniawan et al., 2018).

Sustainability development is crucial for companies, requiring attention to the triple bottom line framework, which emphasizes profits, community well-being (people), and environmental protection (planet). According to (Idawati & Hanifah, 2022), a sustainability report should continuously disclose information across economic, social, environmental, and corporate governance dimensions. Thus, before drafting such reports, companies must fully understand their operational and business flows to reflect these areas accurately (Du et al., 2017).

The company's value is directly proportional to the share price; if a company's share price has a high value, the company value also has a high value, so market confidence also increases (Sari & Irawati, 2022). The selling value of a company in an operating business can also be considered as firm value (Yulianty & Nugrahanti, 2020). So, it can be concluded that firm value is the market value reflected in the movement of stock prices daily. Positive stock movements will encourage investors to be able to invest in the company. In this study, company value is measured by Tobin's Q. This ratio was developed by Professor James Tobin by comparing market and book equity values. Tobin's Q represents investors' perception of the company's value against its book value. Tobin's Q also reveals a company's previous value and considers the prospects for increasing a company (Ammer et al., 2020). In addition, calculations using Tobin's Q are more widely chosen because they are not affected by managerial manipulation and different accounting methods compared to other methods (Swarnapali, 2020).

Institutional ownership is shared ownership by private institutions, both domestic and foreign, as well as government institutions. The purpose of institutional ownership is to monitor or supervise policies made by company managers (Idawati & Hanifah, 2022).

Sustainability Report on Company Value

Research by Shalihin et al. (2020) indicates that sustainability reporting positively impacts firm value. In contrast, Amalia & Yuniarwati (2023) found that sustainability reports either negatively influence or do not significantly affect firm value. Given these conflicting findings, the authors propose further investigation into the effect of sustainability reporting on firm value, formulating the following hypothesis.
H1: Sustainability reports have a positive effect on firm value.

Institutional Ownership Moderates the Effect of Sustainability Reports on Firm Value

Institutional ownership serves a critical supervisory role over management, influencing firm value positively (Sakawa & Watanabel, 2020). Research by Sari & Irawati, (2022) further supports this, indicating that higher levels of institutional ownership correlate with increased firm value. Based on these findings, the study proposes to test the following second hypothesis:
H2: Institutional ownership moderates the effect of sustainability reports on firm value.

Based on the details provided, the research model employed in this study is structured as follows.

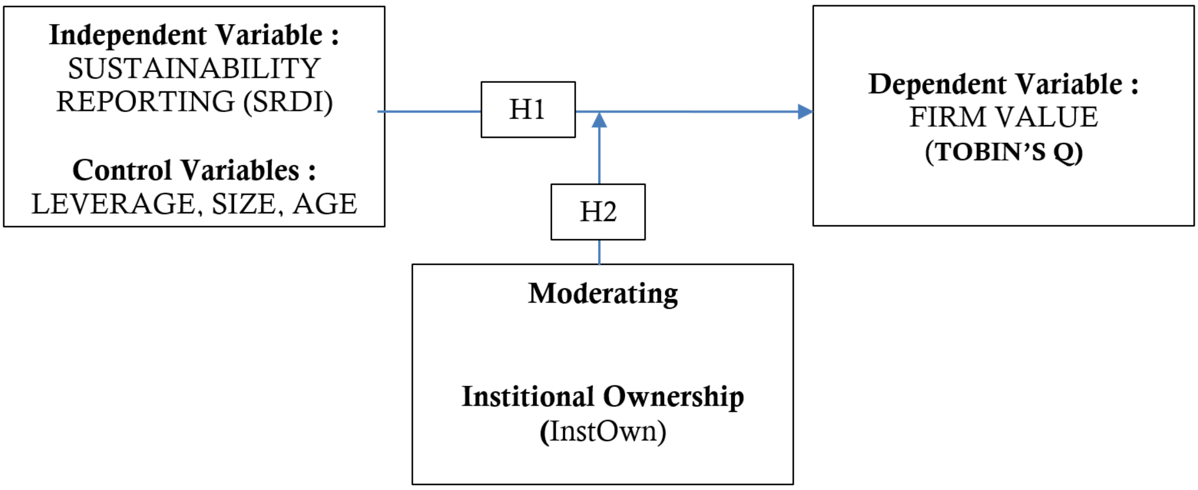

Figure 1. Research Model

RESEARCH METHODS

This research draws on secondary data from financial and sustainability reports of companies listed on the Indonesia Stock Exchange (IDX) from 2017 to 2020. The data were accessed via the official IDX and respective companies' websites. Using purposive sampling, the study targets non-financial sector companies that meet specific criteria: they must be listed on the IDX between 2017 and 2020, consistently publish sustainability reports adhering to GRI standards during the same period, and have issued financial reports annually from 2017 to 2020. This approach identified 39 companies, leading to 156 observation points for the study. Data analysis was performed using a panel data regression model implemented in STATA 17 software.

The independent variable in this study, the sustainability report, encompasses economic, environmental, and social dimensions and is quantified using the Sustainability Report Disclosure Index (SRDI) based on the Global Reporting Initiative (GRI) standards. According to (Agustina et al., 2020), each disclosed item within the report receives a score of 1, while undivulged items score 0. These scores are aggregated to produce an overall SRDI score for each company.

$$SRDI = \frac{Total\ item\ disclosed}{Total\ item\ expected\ to\ be\ disclosed} \quad \ldots\ldots (1)$$

The dependent variable in this research is firm value, measured using Tobin's Q calculation method. Ammer et al. (2020) endorse this method for its ability to reflect investors' perspectives on a company's market value relative to its book value. Tobin's Q is favored because it accounts for potential risks, adapts well to changes in accounting systems, and provides a forward-looking assessment of company value. According to Kurniawan et al. (2018), Tobin's Q formula is applied to assess the firm value.

$$TOBIN'SQ = \frac{Equity\ Market\ Value\ (EMV)}{Equity\ Book\ Value\ (EBV)} \ldots\ldots (2)$$

EMV = Share price per share as of December 31 multiplied by the number of shares outstanding
EBV = Total assets minus total liabilities

The moderating variable in this study is institutional ownership. The existence of institutional ownership or institutional ownership with a large share has a high monitoring impact on institutional investors, which can reduce the deviant behavior of managers (Nugrahanti & Puspitasari, 2018). According to Nurleni et al., (2018); and Wijaya et al., (2023) the method used to assess institutional ownership is as follows:

$$InstOwn = \frac{Number\ of\ shares\ owned\ by\ institutional\ investors}{Total\ shares\ outstanding} \ldots\ldots (3)$$

Following previous research on the effect of sustainability reporting on firm value (Ebaid, 2023), the control variables used in this study are leverage, size, and age. The *leverage* ratio compares the company's total debt to total equity and can be used to evaluate how much credit a company has. The greater the debt ratio of a company indicates that the company's shares have a greater risk for shareholders (Jihadi et al., 2021). According to Alarussi & Alhaderi (2018), the formula for *leverage* is:

$$LEVERAGE = \frac{Total\ Liabilities}{Total\ Assets} \ldots\ldots (4)$$

A company's age indicates its ability to sustain operations, compete in the market, and generate profits from its business activities, as discussed by (Susanti & Restiana, 2018). The following formula is used to calculate the company's age:

Age = Year of Observation - Company IPO Date ……(5)

Aligned with the findings of Murhadi et al. (2021), company size in this study is represented by total assets. Jihadi et al. (2021) further specify that company size should be quantified using the natural logarithm of total assets, applying the following formula:

SIZE = ln (Total Asset) ……(6)

According to Xu (2022), panel data regression analysis integrates cross-sectional and time-series data captured across different periods and frequently predicts variables in established sectors. Additionally, using panel data regression necessitates the application of Chow, Hausman, and Lagrange Multiplier tests to identify the most suitable regression model. In this study, the panel data regression model is articulated using the following equation:

$$Y = \alpha + \beta 1\ (X1) + \beta 2\ (X2) + \beta 3\ (X3) + \beta 4\ (X4) + \beta 5\ (X5) + \boldsymbol{\varepsilon} \ldots\ldots (7)$$

Note:
Y: Firm Value (Tobin's Q); α: Constanta; β1 – β4: Regression Coefficient; X1: Sustainability Report (SRDI); X2: Institutional ownership (InstOwn); X3: Leverage (LEV); X4: Company age (AGE); X5 Company size (SIZE); $\boldsymbol{\varepsilon}$: error percentage.

RESULTS AND DISCUSSION

The research objects used in this study are 39 companies listed on the IDX from 2017 to 2020, and sustainability and financial reports are published consecutively. This analysis explains, describes, and provides information about data based on two large groups of descriptive analysis, namely measures of concentration such as mean, median, and mode, and measures of spread, namely variance and standard deviation. Table 1 is the result of descriptive statistical analysis using STATA 17.

Table 1.
Descriptive Statistics

Variable	Max	Min	Mean	Deviation Std.	N	Skewness
Tobin's Q	1.9870	0.2659	0.7767	0.4109	156	0.6415
SRDI	0.7415	0.0561	0.3250	0.1461	156	0.6278
InstOwn	0.3700	0	0.1113	0.0878	156	0.9881
LEV	0.7998	0.3555	0.6511	0.1114	156	-1.1631
AGE	3.4549	0.2464	2.6780	0.6369	156	-0.8044
SIZE	33.4945	28.3762	30.7993	1.0657	156	-0.2647

The Chow test results show significant results, so based on this test, the model is a Fixed Effect model. Furthermore, the Hausman test was carried out with insignificant results; it was determined that the random effect was better. Furthermore, testing with Lagrange shows significant results, so the model to be interpreted is the random effect model.

The coefficient of determination, represented by the R-squared value, quantifies how much of the variation in the dependent variable is explained by the independent variable(s). A value close to zero indicates that the independent variable has very limited explanatory power regarding the dependent variable's variation. Conversely, a value close to one suggests that the independent variable nearly fully accounts for the variation in the dependent variable. Through data analysis conducted using STATA 17, the obtained R-squared value, as detailed in Table 2, measures the extent to which the independent variables explain the variation in the dependent variable.

Table 2.
Regression Processing Results

Tobin's Q	**Coef.**	**Std. Err**	**z**	**p-value**	**[95% Conf. Interval]**	
SRDI	0.5699**	0.2531	2.2500	0.0240	0.0737	1.0660
InstOwn	0.9843	0.5920	1.6600	0.0960	0.1760	2.1447
SRDI*InstOwn	-0.5875	0.9054	-0.6500	0.5160	-2.3623	1.1871
LEV	0.9977**	0.4240	2.3500	0.0190	0.1665	1.8288
SIZE	-0.0205	0.0505	-0.4100	0.6840	-0.1195	0.0784
AGE	-0.0693	0.0805	-0.8600	0.3890	-0.2271	0.0884
_cons	0.6806	1.4930	0.4600	0.6480	-2.2456	3.6070
Overall R- squared = 0.1284						
Prob > F = 0.0116						

*,**,***Significant at 10, 5 and 1 percent

From the analysis, the overall R-squared value is 0.1284, which translates to 12.84%. This indicates that the sustainability report as the independent variable, accounts for 12.84% of the variance in firm value. Therefore, the ability of the sustainability report to explain changes in firm value is 12.84%, with the remaining variance attributable to other independent variables not included in this study.

The SRDI variable positively and significantly impacts company value, with a 5% significance level, conforming hypothesis 1. This suggests that higher-quality sustainability report disclosures result in better firm value. Investors and capital owners favorably perceive high-quality disclosures about environmental, social, and economic impacts (Shalihin et al., 2020). This conclusion is consistent with findings by Swarnapali (2020) and Zakarias & Bimo (2021), who noted that a better sustainability report increases firm value.

In addition to explaining economic performance, companies also need to explain in detail the standard ratio of employee wages, the proportion of senior management from the surrounding community, significant economic impacts and infrastructure investments, the ratio of company spending on local distributors, legal measures taken by local companies, legal measures taken by companies related to anti-competitive behavior, *anti-trust* practices, and monopolies, as well as disclosures related to anti-corruption and taxes. From this economic category, it can be concluded that in addition to being oriented towards fulfilling profits, companies also pay attention to other aspects, including codes of ethics. If the company generates profits but does not comply with legislation, it will be fatal to the sustainability of the company.

In the environmental category, companies need to explain the raw materials used by the company, energy consumption, water and waste management and treatment, biodiversity, the emissions produced during the company's operations, and how the company can reduce emissions and prevent impacts that may arise from company activities. Companies as economic actors are not only centered on *profit* but must also pay attention to aspects of *people* and the *planet*. Therefore, with the disclosure in the environmental category, companies are invited to be responsible for their business activities, especially those that can potentially damage the environment. Detailed disclosure on environmental aspects can be attractive, especially for investors, and increase public trust because companies are considered capable and take a role in fulfilling their obligations to protect and preserve the earth.

In this category, the company discloses employment and labor that shows that workers continue to get their rights, such as remuneration by regulations and laws, the right to leave, and get bonuses and benefits. In addition, companies also need to disclose that workers have equal opportunities regardless of gender and have the right to express opinions without discrimination. This category asks companies to disclose policies regarding underage workers or incidents of forced labor. Not only that, this category also reveals that companies need to pay attention to *soft skills* and provide *up-to-date* knowledge to their workers so that with training, workers' performance increases, impacting firm value.

Institutional ownership positively affects firm value (significance 10%). This indicates that the higher the percentage of share ownership by institutional investors, the higher the firm value. This result is in line with previous research, which states that the control function of institutional ownership aligns management actions with shareholders (Sakawa & Watanabel, 2020). Additionally, the institutional ownership variable (InstOwn) does not moderate the effect of sustainability reporting on firm value, with a significance level of 10%, not supporting hypothesis 2. This indicates the impact of sustainability reports on firm value between companies with high and low institutional ownership is the same. This explanation aligns with Lavin & Montecinos-Pearce's (2021) research, which did not find the effect of institutional ownership on the quality of sustainability report disclosure and firm value (Sihombing et al., 2023). These two studies indicate that institutional ownership does not affect the quality of sustainability reporting, which impacts increasing company value. Institutional ownership directly influences company performance but does not moderate the effect of sustainability reporting quality on company value; it can be caused that the supervisory mechanism is more direct to financial performance, not yet on how non-financial performance affects company value.

The regression results of the control variable, the leverage variable, significantly affect firm value. These results align with research conducted by (Nguyen, 2020). This result can be explained because, conceptually, using debt to finance the purchase of company assets raises tax shields that increase company profits (Abdi et al., 2022). Investors react positively to positive earnings information so that the company value increases.

Company size (SIZE) and age (AGE) do not affect firm value. No effect of company size on firm value was found, which aligns with the research (Bon & Hartoko, 2022). According to their study, this result shows that capital owners need to consider the company's size based on total assets rather than on other factors, such as how management manages the assets owned to improve the company's financial performance. In line with the research of Girón et al. (2021), no effect of company age on firm value was found. The age of the company or how long the company has been listed as a public company has no impact on the firm value; investors and creditors see other aspects, such as profitability, compared to the company's age. This can be interpreted because the research sample uses the financial statements of the year when the COVID-19 pandemic caused certain sectors to experience a downturn so that the firm's value is more determined by the business sector rather than the company's age. The emergence of new businesses causes investors and creditors to focus on financial conditions rather than the company's age listed on the stock exchange.

In general, the findings of this research imply that if the value of the sustainability report gets bigger, the company value also gets higher (directly proportional) and vice versa. According to legitimacy theory, companies that carry out *social disclosure* are considered to have social status/labels from the surrounding community and society so that the company's entity is considered valid. Jawas & Sulfitri (2022) argue that the perspective of legitimacy is that there is pressure on companies with strong social capabilities and links to the environment to show great commitment in reporting activities to get the company's endorsement of society. So, the sustainability report prepared and published by the company can be a solution for companies to improve their image and obtain legitimacy from the community, *stakeholders*, and regulators. Companies with a positive image from the community tend to get a positive response from investors, so they have the potential to increase the value of the company's shares, which impacts the company value of the related company. The following is a comprehensive description of the economic, environmental, and social categories of the sustainability report.

CONCLUSION

Based on the analysis and discussion of research data, it is evident that sustainability reports positively impact firm value, indicating that higher quality sustainability reporting correlates with increased company value. Additionally, institutional ownership does not moderate the relationship between sustainability reports and firm value; there is no difference in the effect of sustainability reporting on firm value in high institutional ownership with low institutional ownership.

The empirical evidence found in this study has theoretical implications, and it enriches similar studies that find that the quality of sustainability reporting disclosure is a factor that determines the company's value. The completeness of information and transparency of sustainability reporting are considered positive in making investment decisions by capital owners. The practical implication of this research is that management needs to strengthen completeness and transparency following the sustainability reporting standards used in Indonesia. The more complete the information presented, the higher the investor evaluates the company.

For further research, it is recommended to conduct a peer review when carrying out the calculation and assessment process on the disclosure of sustainability reports published by sample companies to obtain valid, objective results by predetermined standards. Furthermore, research companies in similar sectors to obtain results in real conditions and see the effect of sustainability reports on firm value by the characteristics of companies in each sector.

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