Etikonomi
Volume 22 (1), 2023: 65 - 78
P-ISSN: 1412-8969; E-ISSN: 2461-0771

Environmental, Social, Governance and Firm Performance in Developing Countries: Evidence from Southeast Asian

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JEL Classification:
G30
Q56
Q50

Received: 21 March 2022

1st Revision: 25 April 2022

2nd Revision: 19 June 2022

Accepted: 01 August 2022

Abstract
Several studies primarily investigate the influence of environmental, social, and governance on firm performance in a developed country where markets have matured, and investors are aware of corporate social responsibility activities. Therefore, studies in developing countries are still rare and mixed. This study examines the effect of Environmental, Social, and Governance (ESG) information on firm performance in ASEAN developing countries. We observed companies in ASEAN developing countries (Indonesia, Malaysia, Philippines, Thailand, and Vietnam) during 2010-2020. The information on ESG score and ROA as a proxy for firm performance measures ESG. Regression test results showed that ESG has a positive effect on firm performance. We also found that three components of ESG, environmental, Social, and Governance, positively affect firm performance. Robustness test results showed that overall ESG information, environmental information, and social initiatives affect the firm's market performance (Tobin's Q). Research originality in this study proves that developing countries have a positive effect between ESG disclosure and company performance. ESG, in the long term, would build effective governance and increase shareholder value. The research implication is to suggest a company has ESG information due to empirical testing that ESG information enhances a firm operational and market performance.

Keywords:
sustainability; environment; corporate governance; social; firm performance

How to Cite:

Makhdalena., Zulvina, D., Zulvina, Y., Amelia, R. W., & Wicaksono, A. P. (2023). Environmental, Social, Governance, and Firm Performance in Developing Countries: Evidence from Southeast Asian. *Etikonomi, 22*(1), 65–78. https://doi.org/10.15408/etk.v22i1.25271.

INTRODUCTION

Enhancing firm performance is always a concern for companies. Several studies have tested the factors that can improve firm performance (Yoo & Managi, 2021; Qoyum et al., 2021; Bodhanwala & Bodhanwala, 2021; Bhaskaran et al., 2021; Alareeni & Hamdan, 2020), and one of them is environmental, social, and governance (ESG) information increase firm performance (Mohammad & Wasiuzzaman, 2021; Yoo & Managi, 2021; Alareeni & Hamdan, 2020). Sustainable value like ESG information is created by sustainable financial institutions focusing on long-term financial and economic benefits (Bhaskaran et al., 2021). Because of increasing stakeholder expectations, corporations must manage their societal impacts, including human rights, labor, and diversity. Therefore, corporate sustainability entails respect for universal principles in these areas and proactive support of a sustainability agenda. An interconnected environment nowadays is characterized by ESG, networks of people, organizations, and devices continuously interacting, conversing, and exchanging information in indicating information sharing, signaling, and brand value creation have evolved in the past decade (Lee et al., 2022). Qoyum et al. (2021) test firms in Indonesia and Malaysia, two emerging countries in ASEAN (Association of Southeast Asian Nations), reveals that firms labeled Islamic have better environmental and social performance but not governance performance.

A firm sustainability report is considered an effort of transparency and accountability that can measure the company's concern for sustainability (Kim et al., 2018). ESG does not only consider environmental and social factors but also involves aspects of corporate governance. This condition is because managers and stakeholders worldwide perceive that corporate governance is an issue along with encouraging global economic growth and significant growth (Singh & Gaur, 2009). In addition, governance can also be used to assist decision-making related to corporate governance (Singh & Gaur, 2013). Atan et al. (2018) define the three aspects of ESG, namely: environmental aspects related to nature protection, climate change, and environmental impacts resulting from business operations; social aspects related to issues such as equality, diversity in the workplace, human rights, and corporate social contribution; and governance aspects related to board independence, ownership structure, minority shareholder rights, fair treatment of shareholders, and transparency of company information. Environmental and social activity assessment indicators and management mechanisms are still crucial for businesses and other stakeholders (Abughniem et al., 2019).

The environmental aspect addresses many issues related to the business and community environment (e.g., CO_2 emissions, energy consumption, energy efficiency policies, total waste, and emission reduction policies) (Alareeni & Hamdan, 2020). Several studies have shown a positive influence between the environment and firm value (Yoo & Managi, 2021; Qoyum et al., 2021; Alareeni & Hamdan, 2020).

The social aspect contains social information such as gender, number of employees, turnover ratio, human rights, product safety, the ratio in management, and the ratio of female employees (Alareeni & Hamdan, 2020). Yoo & Managi (2021) found that corporate social scores positively affect company performance. Companies are starting

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DOI: https://doi.org/10.15408/etk.v22i1.25271

to realize and consider corporate social responsibility practices as a driver of company market performance (Alareeni & Hamdan, 2020).

The governance aspect reflects issues related to the corporate governance structure (such as board independence, corruption, bribery, reporting and management, and shareholder protection). Alareni & Hamdan (2020) find that higher governance practices improve and positively affect operational and market performance. Companies that adopt governance mechanisms will provide more helpful information to investors and other users of financial statements to reduce the asymmetry of information (Alareeni & Hamdan, 2020). The reputation of corporate social responsibility (CSR) is considered a valuable tangible resource that can provide long-term benefits for the company (Lourenço et al., 2014).

Providing disclosure on ESG aspects is essential to increase company value and show the company's resilience and sustainability (Melinda & Wardhani, 2020). Mohammad & Wasiuzzaman (2021) investigated the influence of ESG on firm performance in one of the ASEAN developing countries, Malaysia, and found that ESG improves firm performance. They said the company's disclosure of sustainability efforts could help efficiently manage its resources and increase its value. ESG factors tend to treat them either as a way to attract socially responsible asset owners or as a tool to reduce their portfolio companies' regulatory or reputational risks. Their finding claim that Malaysian firms that disclose their ESG efforts are found to generate long-term performance throughout this study.

Alareeni & Hamdan (2020) found that the higher disclosure of ESG enhances the firm's operations. This condition may be because the yearly variation of the ESG disclosure increases the positive image of firms and then performance. ESG performance could mitigate financial risk during a financial crisis (Broadstock et al., 2020). Buallay (2018) found that disclosing more information about ESG enhances a company's performance. Buallay (2018) also found in each pillar of ESG that the environment positively impacts firm performance, but social and governance disclosure negatively affects firm performance. It indicates that social disclosure develops because executive management and boards of directors work on social policies for their benefit (Buallay, 2018). If so, then three possible outcomes are that these policies result in costs to the banks, costs that are borne by stakeholders, which lower the market value (TQ), the equity (ROE), and the efficiency of assets (ROA) (Buallay, 2018).

Atan et al. (2018) showed that ESG does not affect firm performance. Bodhanwala & Bodhanwala (2021) also showed that corporate environmental performance has no significant effect on firm performance (ROA). They also found that corporate social performance has a negative effect on ROA. Meanwhile, corporate governance has a positive relationship with firm performance. Khan et al. (2021) found that green process innovation negatively affects returns on assets (ROA). This negative relationship is because the shift in processes and services requires enormous investment. Ruan & Liu (2021) found that corporate ESG activities significantly negatively impact firm performance in China. They assumed that in emerging market countries where ESG activities are inactive, the ESG information disclosure requirements for listed companies might evolve into a severe cost burden, leading to a significant negative correlation between ESG ratings and firm performance.

Researchers studied the association between corporate social responsibility and financial performance primarily based in developed countries where markets are mature, and investors are well aware (Fahad & Busru, 2021). Studies in developed countries find that the positive association between performance and ESG disclosure is due to lower information risk associated with higher disclosure of ESG (Cormier & Magnan, 2007). Firms that engage in ESG disclosures in the developed market are associated with lower systematic market risks and idiosyncratic risks due to a lower possibility of litigation or adverse market reaction (Sassen et al., 2016). Fahad & Busru (2021) investigated the effect of CSR on firm performance of emerging markets listed in the BSE 500 index India and they found that the negative effect of CSR disclosure on firm profitability and firm value in India, this negative effect is mainly influenced by environmental disclosure score and social disclosure score.

A study suggests that ESG disclosures reduce information asymmetry and improve investors' perception and recognition of the firm's investment strategies (Fatemi et al., 2018). Contrast findings found by Ting et al. (2019) that emerging market firms had higher ESG initiatives regarding resource use, workforce, human rights, and CSR strategies. Besides that, they found that ESG initiatives might lead to significant improvements in firm valuation effects. Mohammad & Wasiuzzaman (2021) said that in an emerging market, value creation through integrating ESG in a firm's long-term strategy with the right vision would attract the best talent, build authentic customers via effective governance structure and increase shareholder value. Therefore, studies on ESG in emerging markets still need to be completed (Mohammad & Wasiuzzaman, 2021).

Baughn et al. (2007) mentioned that the diverse characteristics of a country have a significant role in explaining the CSR practice, like culture, population, and country's lifestyle. Bhatia & Makkar (2019) found that companies in developed economies give less priority to community issues, and companies in developing countries are producing CSR information either in annual reports or in separate stand-alone CSR reports, but it needs more reliability and transparency.

Due to the impact of the US-China trade war, thereby moving all or part of their production lines to Southeast Asia, ASEAN became an investment destination country. Investors need further information regarding business activities, not only limited to financial information but also non-financial information involving aspects, such as ESG (Atan et al., 2018). Emerging market countries like developing countries in ASEAN are still in the early stages of economic development to pay more attention to the scale and speed of economic growth and related financial indicators, which often lead to neglect of ESG issues (Ruan & Liu, 2021). This study investigates the influence of environmental, social, and governance information on firm performance in developing countries in ASEAN. This research contributes to the research context in ASEAN developing countries.

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DOI: https://doi.org/10.15408/etk.v22i1.25271

Prior studies have examined the association between ESG and firm performance. Clark et al. (2015) mentioned that there are common types of ESG studies that have been published. The scholars have directly examined individual dimensions of ESG (e.g., governance), testing for correlations with firm performance, and claimed that 85 percent of ESG studies only examine one aspect of ESG and not all three aspects simultaneously. Another contribution of this research is that we investigated the ESG impact on firm performance and examined all three dimensions of ESG and its impact on firm performance.

METHODS

This study examines the effect of ESG and its components on firm performance in ASEAN: Indonesia, Malaysia, Philippines, Thailand, and Vietnam. This research uses data from 2010 until 2020. The research sample was taken based on the companies listed on the stock exchanges of each country and collected by the Thomson Reuters database. The final total of the research sample was 1418 observations per firm-year. Table 1 presents research sample information.

Table 1. Research Sample

Country	Freq.
Indonesia	338
Malaysia	488
Philippines	203
Thailand	384
Vietnam	5
Total	**1418**

Our research data is an unbalanced data panel. Research data was collected from the Thomson Reuters database, the company's website, and the website of the world bank. The dependent variable is the firm performance measured by firm profitability, namely return on assets (ROA) or the ratio of net income divided by total assets of book value (Buallay, 2018). ROA data were collected from the Thomson Reuters database. The independent variable of the study is ESG and each of its components, namely Environmental, Social, and Governance which is measured using ESG scores collected from the Thomson Reuters database (Velte, 2019).

The research uses leverage, firm size, firm age, and gross domestic product (GDP) control variables. Leverage is measured by the ratio of total debt to company equity. Leverage data is collected from the Thomson Reuters database. Company size is measured using the logarithm of the company's total assets. This data is taken from the Thomson Reuters database. The company's age is the length of the company since it was founded. Company age information is obtained from the website of each company. The control variable GDP is used to control for country variations in the study. GDP is measured by the logarithm of each country's GDP each year. GDP information is obtained from the website of the world bank. Table 2 presents the operationalization of research variables.

Table 2. Operationalization of Research Variables

Variable	Definition	Measurement	Source
Firm Performance (ROA)	Firm profitability is measured by the ratio of net income divided by total assets of book value (Buallay, 2018).	Net income/total asset	Thomson Reuters Database
ESG Information (ESG)	Environmental, social, and governance performance scores were collated by the Asset4 database by Thomson Reuters (Velte, 2019)	ESG Score (Alareeni & Hamdan, 2020)	Thomson Reuters Database
Environmental (ENV)	Environmental performance score collated by the Asset4 database by Thomson Reuters (Velte, 2019)	Environmental Score (Alareeni & Hamdan, 2020)	Thomson Reuters Database
Social (SOC)	Social performance obtained from Asset4 (Velte, 2019)	Social Score (Alareeni & Hamdan, 2020)	Thomson Reuters Database
Governance (GOV)	Governance performance obtained from Asset4 (Velte, 2019)	Skor governance (Alareeni & Hamdan, 2020)	Thomson Reuters Database
Leverage (LEV)	The ratio of total debt divided by total equity (Khalil *et al.*, 2019)	$LEV = \frac{Debt}{Equity}$ (Khalil *et al.*, 2019)	Thomson Reuters Database
Firm Size (SIZE)	Natural logarithm of total assets (Velte, 2019)	SIZE = Ln(total asset) (Liao *et al.*, 2015)	Thomson Reuters Database
Firm Age (AGE)	Firm age since established	Firm age since established	Company's Website
Gross Domestic Product (GDP)	The total of all value-added created in an economy	GDP = Ln(GDP)	World Bank Website

This study examines four research models by testing each independent variable on the dependent variable. We defined our variables' relationship in Figure 2.

$$ROA_{it} = \alpha + \beta_1 ESG_{it} + \beta_2 LEV_{it} + \beta_3 SIZE_{it} + \beta_4 AGE_{it} + \beta_5 GDP_{it} \quad (1)$$

$$ROA_{it} = \alpha + \beta_1 ENV_{it} + \beta_2 LEV_{it} + \beta_3 SIZE_{it} + \beta_4 AGE_{it} + \beta_5 GDP_{it} \quad (2)$$

$$ROA_{it} = \alpha + \beta_1 SOC_{it} + \beta_2 LEV_{it} + \beta_3 SIZE_{it} + \beta_4 AGE_{it} + \beta_5 GDP_{it} \quad (3)$$

$$ROA_{it} = \alpha + \beta_1 GOV_{it} + \beta_2 LEV_{it} + \beta_3 SIZE_{it} + \beta_4 AGE_{it} + \beta_5 GDP_{it} \quad (4)$$

Where:

ROA : Firm Performance

ESG : Environmental. Social, and Governance

ENV : Environmental

SOC : Social

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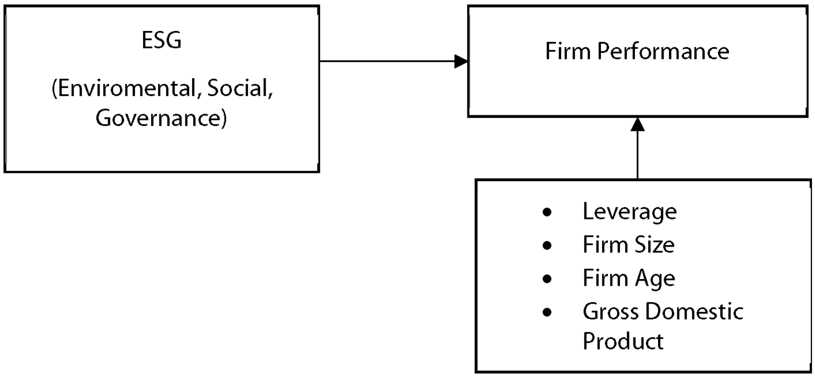
DOI: https://doi.org/10.15408/etk.v22i1.25271

GOV: Governance
LEV : Leverage
SIZE: Firm Size
AGE : Firm Age
GDP: Gross Domestic Product

Figure 2. Research Framework



RESULT AND DISCUSSIONS

Descriptive Statistics

Descriptive statistics result is presented in table 3. The mean score of ROA is 0.079, with a minimum score is -0.423, and a maximum score is 1.149. The average ESG score is 44.98. This score is in grade C. Grade 'C' indicates satisfactory relative ESG performance and a moderate degree of transparency in reporting material ESG data publicly (Refinitiv, 2021). The maximum ESG score is 89.73. This score is in grade A. Grade 'A' indicates excellent relative ESG performance and a high degree of transparency in reporting material ESG data publicly. ESG's minimum score is 2.77. This score is in grade D. Grade 'D' indicates poor relative ESG performance and an insufficient degree of transparency in reporting material ESG data.

Table 3. Descriptive Statistic

Variable	Mean	Std. Dev.	Min	Max
ROA	0.079	0.098	-0.423	1.149
ESG	44.987	19.583	2.77	89.73
ENV	36.448	25.083	0	97.15
SOC	48.752	23.362	0.71	97.35
GOV	47.734	21.636	3.04	98.7
LEV	1.68	2.558	0.002	49.223
SIZE	31.39	1.116	27.763	34.712
AGE	40.334	27.786	1	186
GDP	26.849	0.461	26.048	27.744

The average environmental score (ENV) is 36.44, with a minimum score of 0 and a maximum score of 97.15. the average environmental information is in grade C. This result also showed that some companies had not disclosed their environmental information. Therefore 0 scores are assigned to them (minimum score of ENV). The average social score (SOC) is 48, with a minimum score of 0.71 and a maximum score of 97.35. This average GOC score is also in grade C. Average governance score (GOV) is 47.73, with a minimum score of 3.04 and a maximum score of 98.7. The average score of GOV is in grace C too.

Regression Result

Table 4 shows the results of the regression test. Table 4 model 1 showed that ESG has a significant positive effect on firm performance (ROA) with a significant level of 0.041. It indicates that better ESG information increases firm performance. This result aligns with prior research showing that ESG disclosure positively affects firm performance (Buallay, 2018; Velte, 2019; Alareeni & Hamdan, 2020). There may be a positive relationship between ESG and ROA because the yearly variation of the ESG disclosure enhances the positive image of firms and then their performance (Alareeni & Hamdan, 2020).

Table 4. Regression Results

	ROA			
	(1)	(2)	(3)	(4)
ESG	0.000384** (0.041)			
ENV		0.00029365** (0.020)		
SOC			0.000304** (0.026)	
GOV				0.000234** (0.029)
LEV	-0.003663*** (0.000)	-0.003768*** (0.000)	-0.003763*** (0.000)	-0.003884*** (0.000)
SIZE	0.000 (0.988)	-0.027394*** (0.000)	-0.02661*** (0.000)	-0.025341*** (0.000)
AGE	0.001 (0.921)	0.000526*** (0.002)	0.000534*** (0.000)	0.000537*** (0.002)
GDP	0.086590* (0.052)	0.029733*** (0.005)	0.028494*** (0.006)	0.028980*** (0.006)
YEAR	yes	yes	yes	yes

**** p<.01, ** p<.05, * p<.1*

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DOI: https://doi.org/10.15408/etk.v22i1.25271

The results also found that each component of ESG, namely environmental, social, and governance information, positively influences firm performance. It means ENV increases firm performance (ROA). Model 2 showed that ENV has a significant positive relationship with ROA with a significant level of 0.020. Model 3 showed that SOC significantly positively affects ROA with a significant level of 0.026. That means social information can enhance firm performance. Model 4 showed that GOV has a significant positive effect on ROA with a significant level of 0.029. It means governance information could improve firm performance.

These results found that ESG and its three-pillar components, namely, environmental, social, and corporate governance information, positively affect firm performance. These results are consistent with Velte (2019) research that the three pillars of ESG, namely environmental, social, and governance, positively affect firm performance (ROA). Alareeni & Hamdan (2020) mentioned that firms with high ESG, EVN, and CSR disclosure levels have higher operational and financial performance (ROA). This evidence showed that ESG and its three pillars have a significant and valuable factor for firm performance in ASEAN companies.

Firm disclosure of sustainability efforts can help efficiently manage its resources and increase its value (Mohammad & Wasiuzzaman, 2021). ESG factors tend to treat them either as a way to attract socially responsible asset owners or as a tool to reduce their portfolio companies' regulatory or reputational risks. Companies that adopt governance mechanisms will provide more helpful information to investors and other users of financial statements to reduce asymmetry information (Alareeni & Hamdan, 2020). ESG performance could mitigate financial risk during a financial crisis (Broadstock et al., 2020). Buallay (2018) also found that disclosing more information about ESG could enhance firm performance.

ESG factors and their components, environmental, social, and governance factors, represent a company's non-financial performance. This information invites investors to consider ESG issues when evaluating firm performance (Atan et al., 2018). Better ESG disclosure helps companies increase their corporate performance, create a good image and credibility and promote corporate ethical practices (Kumar & Firoz, 2022). Fischer & Sawczyn (2013) found a positive relationship between corporate social performance and financial performance (ROA) and concluded is affected by the degree of innovation. The better ESG-performing firms have good firm performance (Chelawat et al., 2016) and ESG effects on firm valuation (Fatemi et al., 2017). ESG helps investors assess a company's behavior and determine the company's future financial performance (Ting et al., 2019).

ESG disclosure is a crucial way to report non-financial information, providing stakeholders with a stable flow of valuable data and information and reducing information asymmetry (Ellili, 2022). This condition reduces transaction costs and distribution competition between key stakeholders, provides a competitive advantage in procuring and using environmental resources, and ultimately positively impacts corporate value (Ruan & Liu, 2021). Moreover, from a resource-based theory and strategic management perspective, ESG activities can create a unique competitive advantage for a company (Ruan

& Liu, 2021). The reputation of a sustainability report is considered a valuable tangible resource that can provide long-term benefits for the company (Lourenço et al., 2014).

We found that social information has a positive effect on firm performance. This result is consistent with Yoo & Managi (2021) found that corporate social scores positively affect company performance. Companies are starting to realize and consider corporate social responsibility practices as a driver of company market performance (Alareeni & Hamdan, 2020). Social responsibility is fundamental and relevant in science and business management (Ting et al., 2019). The Principles control approximately 50% of the world's institutional asset base for Responsible Investment signatories, demonstrating the financial market's commitment to adopting ESG standards for investment decisions (Ting et al., 2019).

The result also showed that better governance information could increase firm performance. This result supported the literature by Alareni & Hamdan (2020) that higher governance practices improve and positively affect operational and market performance. Companies that adopt governance mechanisms will provide more helpful information to investors and other users of financial statements to reduce asymmetry information (Alareeni & Hamdan, 2020). The results also showed that the control variables of research, which are leverage and firm size, hurt firm performance, but firm age and GDP positively affect firm performance. This finding indicates that smaller companies and leverage have greater performance rather than larger companies. It also indicates that the older company does more to improve the firm performance

Robustness Test

Table 5 shows the result of the robustness test. Using Tobin'sTobin's Q, we measured firm performance with market value (Buallay, 2018; Alareeni & Hamdan, 2020; Ting et al., 2019). Robustness test results showed that ESG positively impacts market firm performance. Environmental and social pillars have a positive effect on market firm performance. Meanwhile, governance does not affect market firm performance. This finding consists of our regression result that ESG positively impacts firm performance measured by ROA. The result found that governance information does not impact a on firm's market performance, indicating that there is no significant effect on firm value creation if the company discloses the information on firm governance (such as management, shareholders, and CSR strategy).

The robustness test result also showed that environmental and social information could enhance firm market performance. It indicates that the higher disclosure of overall ESG, environmental, and social information enhances a firm's market performance. This condition may be because the yearly variation of the ESG disclosure enhances the positive image of firms and then their performance (Alareeni & Hamdan, 2020). ESG initiatives may significantly improve valuation effects (Ting et al., 2019). Firms with higher environmental initiatives can improve shareholders' wealth, and social initiatives lead to value creation (Ting et al., 2019).

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DOI: https://doi.org/10.15408/etk.v22i1.25271

Table 5. Robustness Test Result

	Tobin's Q			
	(1)	(2)	(3)	(4)
ESG	0.005205* (0.076)			
ENV		0.0070849*** (0.003)		
SOC			0.007144*** (0.005)	
GOV				0.000 (0.895)
LEV	0.002	0.006	0.007	0.001 (0.969)
SIZE	-0.52076***	-0.786046*** (0.000)	-0.762757*** (0.000)	-0.48500*** (0.000)
AGE	-0.096	0.017193*** (0.000)	0.017361*** (0.000)	0.100 (0.601)
GDP	1.96799***	0.654648*** (0.011)	0. 637300*** (0.014)	1.8958433*** (0.010)
YEAR	yes	yes	yes	yes

***** p<.01, ** p<.05, * p<.1**

This result contradicts the finding by Ruan and Liu (2021), who assumed that in emerging market countries where ESG activities are not active, the ESG information disclosure requirements for listed companies might evolve into a severe cost burden for these companies, thereby leading to a significant negative correlation between ESG ratings and firm performance.

CONCLUSION

Increasingly visible environmental and risk issues have made more regulatory agencies and enterprises aware of the importance of environmental, social, and governance (ESG) activities. This study examines the effect of company environmental, social, and governance (ESG) information on firm performance. The study's results found that overall ESG information can improve company performance. The three ESG pillars of environment, social, and governance show similar results, positively impacting corporate performance. These results indicate that carrying out environmental, social, and corporate governance-related activities and disclosing them is proven to improve firm performance in developing countries' companies in ASEAN. This positive relationship may be due to the year-to-year fluctuations in ESG disclosure, improving the company's positive image and, thus, its performance. The improvement in ESG is attractive to stakeholders because disclosure allows the company to minimize the information asymmetry between the company and its stakeholders and improve its performance. Companies with good ESG exposure gain more stability and resilience regarding operational and financial performance.

This research can be used as academic literature to see the effect of environmental, social, and corporate governance information on company performance. Research findings can also be considered for companies to carry out activities related to environmental, social, and better corporate governance and disclose them to reduce information asymmetry and improve company performance. We also found that ESG information has positive effects on firm market performance. Rather than an expense, managers could consider ESG as an investment. They are addressing the environmental, social, and institutional requirements, and the different stakeholder requirements result in value creation for firms. This research can also be a consideration for regulators to mandate companies to practice environmental, social, and good corporate governance as a form of corporate awareness to be environmentally and socially responsible both inside the company and outside the company, which this activity is empirically proven to improve company performance.

This research has its limitations. This study uses listed companies presented in the Thomson Reuters database in developing Southeast Asian countries, so several developing countries in Southeast Asia are not included in the research observations.

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