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The Impact of ESG Factors on Investment Decisions: Exploring the Interplay between Sustainability Reporting, Corporate Governance, and Financial Performance

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Abstract

ESG (Environmental, Social, and Governance) factors are increasingly a concern in investment decision-making, especially related to their role in influencing financial performance, sustainability reporting, and corporate governance. With a mixed method approach, this study combines quantitative and qualitative analysis to explore the relationship between these variables comprehensively. Quantitative analysis uses data from companies' annual reports, ESG scores published by rating agencies, as well as financial data from companies listed on the stock exchange. The results of regression analysis and Structural Equation Modeling (SEM) show that ESG significantly affects financial performance, with corporate governance as a mediator that strengthens this relationship. In addition, sustainability reporting has been shown to increase investor confidence through increased transparency. On the qualitative side, in-depth interviews with investment managers and financial analysts provide insight that while ESG is considered important in investment decision-making, there are challenges in its implementation, including the diversity of reporting standards and long-term impact measurement. These findings underscore the importance of integrating ESG factors in investment strategies to create long-term value while supporting sustainability. The main recommendations are the harmonization of sustainability reporting standards and the strengthening of corporate governance to support the wider adoption of ESG-based investments.

Keywords: *ESG, Sustainability Reporting, Corporate Governance, Financial Performance, Investment Decisions.*

Introduction

In recent decades, sustainability issues have become one of the main concerns in various sectors, including the investment world. ESG (Environmental, Social, and Governance) factors have evolved from mere sustainability indicators to strategic elements that significantly influence investment decision-making. ESG is considered not only as a tool to reflect a company's commitment to sustainability, but also as a measure of long-term performance that is able to manage various non-financial risks, such as reputational risks and operational sustainability. Investors are increasingly aware that companies that excel in managing ESG factors tend to be more resilient to global economic challenges, more innovative, and better able to create sustainable value. Meta-analytical research by Friede et al. (2015) revealed that more than 2000 studies showed a positive relationship between ESG integration and corporate financial performance, confirming the importance of this factor in modern investment decision-making.

ESG (Environmental, Social, and Governance) factors have taken center stage in the modern investment world due to their ability to reflect the value of sustainability and the long-term performance of companies (Fulton et al., 2012). The environmental dimension includes issues such as carbon emission management, the use of renewable energy, waste management, and biodiversity conservation. In the context of investment, companies that successfully manage environmental risks are often considered more stable in the face of global economic challenges, especially in an era where environmental regulations are increasingly strict (Schmidheiny, 1992; Hillary, 2017). Investors see environmental performance as an important indicator in anticipating long-term material risks that could disrupt company operations (Huang et al., 2018).

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Meanwhile, the social dimension focuses on how companies interact with the public, employees, and other stakeholders. Issues such as gender equality, workers' rights, job security, social responsibility, and community impact are of primary concern (Stahl et al., 2020; Torres et al., 2019). Companies that demonstrate a strong commitment to social issues are often better able to build positive reputations and long-term, mutually beneficial relationships with society and customers. In the world of investment, the social dimension can provide added value by creating brand loyalty and reducing the risk of litigation or boycotts that may arise from ethical or social violations (Hunt, 2019; Vogel, 2007).

The last dimension, corporate governance, includes aspects such as the structure of the board of directors, transparency of financial statements, business ethics, and anti-corruption policies (Previtali & Cerchiello, 2023; Wijayati et al., 2016). Strong governance shows that the company has an effective and responsible decision-making mechanism. This not only increases investor confidence but also ensures that the company can face challenges with a strategic and measured approach. In the context of ESG, the governance dimension serves as a foundation that strengthens the implementation of environmental and social policies. Poor governance factors can damage investor confidence even though the company excels in the environmental and social dimensions (Mukhtaruddin et al., 2019). Therefore, these three factors complement each other in providing a holistic picture of a company's sustainability and long-term prospects for investors (Unruh et al., 2016; Wang & Bansal, 2012).

On the other hand, sustainability reporting has become a key tool for companies to communicate their operational impact on economic, environmental, and social dimensions to investors and other stakeholders (Opferkuch et al., 2021). With international standards such as the Global Reporting Initiative (GRI) and the Sustainability Accounting Standards Board (SASB), companies have a framework that allows them to prepare sustainability reports in a transparent and trustworthy manner (ZHALEHAZAD ZANJANI et al., 2023). However, the implementation of sustainability reporting is not without challenges. Differences in reporting standards between countries or sectors, a lack of global harmonization, and limitations in measuring the long-term impact of sustainability initiatives make integrating sustainability reporting into corporate strategies a complex task and requires further attention (Eccles & Serafeim, 2013; Christensen et al., 2019).

In addition, strong corporate governance plays a central role in improving investor confidence and operational efficiency (Shahid & Abbas, 2019; Shahid & Abbas, 2019). Good governance not only ensures corporate transparency and accountability but also helps organizations respond to social and environmental pressures in a more adaptive way. In the context of ESG, corporate governance can serve as a bridge that connects sustainability initiatives with positive financial results. Research by Khan et al. (2016) shows that companies with strong governance tend to have more stable financial performance and are more able to attract investors. However, the relationship between ESG factors, corporate governance, and financial performance is still a topic that needs to be explored further, especially to understand how these interactions affect investment decisions in global financial markets (Tseng et al., 2019; Al-Hiyari et al., 2023).

Based on this background, there are several main questions that are the focus of this research. First, how do ESG factors affect investment decisions? Second, what is the role of corporate governance in strengthening the relationship between ESG and financial performance? Third, how does sustainability reporting affect investors' perception of the company? These questions reflect the complexity and relevance of the topics raised, while also highlighting the need for more in-depth research to answer them.

This research aims to provide a more comprehensive understanding of the above issues. Specifically, this study aims to analyze the impact of ESG factors on investment decisions, explore the role of corporate governance as a mediator between ESG and financial performance, and examine how sustainability reporting can affect transparency and investor confidence. With a holistic approach, this research is expected to make a significant contribution to academic literature and practice in the world of investment. In addition, the research also aims to provide strategic insights for companies in integrating ESG into their business and investment strategies, with the hope of creating sustainable long-term value for all stakeholders (Shome et al., 2023).

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Literature Review

Research related to ESG (Environmental, Social, and Governance) factors in investment decision-making has developed significantly in the last two decades. The study aims to explore the contributions of previous research on the relationship between ESG, sustainability reporting, corporate governance, and financial performance, as well as how these findings are relevant to the research being conducted (Oprean-Stan et al., 2020; Ahmad et al., 2024).

ESG and Investment Decisions

Friede et al. (2015) conducted a meta-analysis of more than 2000 studies examining the relationship between ESG and financial performance. They found that most of the research showed a positive relationship between ESG integration and financial performance, especially in the long term. These results support the view that companies that manage ESG factors effectively are better able to create sustainable value for stakeholders, including investors. However, these findings also show that the impact of ESG on investment decisions is highly dependent on the industry sector and the applicable regulatory framework. In the context of this study, the findings of Friede et al. are relevant because they reinforce the hypothesis that ESG factors can influence investors' preferences towards certain companies.

Sustainability and Transparency Reporting

Eccles et al. (2012) underlined the importance of sustainability reporting in increasing transparency and investor trust. They found that companies that implemented sustainability reporting tended to have better governance and superior financial performance than companies that did not report sustainability. However, Eccles et al. also noted that variations in reporting standards are a major challenge in ensuring the consistency and credibility of the data presented. This research inspired the approach in this study to assess the role of sustainability reporting as a mediator between ESG and investment decisions.

Corporate Governance and Financial Performance

Khan et al. (2016) highlighted the importance of corporate governance in strengthening the relationship between sustainability initiatives and financial results. In their research, good corporate governance was found to be able to mitigate risks stemming from poorly managed environmental and social activities. In addition, the study also shows that strong governance can increase investors' perception of a company's stability and credibility. This study is relevant because it highlights the role of corporate governance as a key element in the conceptual model that will be used in this study.

Cross-Sector Research Framework

Several cross-sector studies, such as those conducted by Clark et al. (2015), show that the effects of ESG on investment decisions can vary depending on the industry sector, the size of the company, and the level of regulatory complexity. The research reveals that sectors such as renewable energy and technology tend to show a greater ESG impact than traditional sectors such as manufacturing. This research is important as a foundation for understanding the heterogeneity of ESG impacts in the context of different sectors, which can be adopted in this study for a more detailed analysis.

Correlation with This Research

Previous research has provided strong insights into the importance of ESG, sustainability reporting, and corporate governance in investment decision-making. However, most studies focus on one aspect of the relationship, without exploring the holistic interactions between the three variables. This research seeks to fill this gap by exploring in depth how ESG factors, sustainability reporting, and corporate governance interact in influencing investment decisions and financial performance. With a mixed method approach, this study will make a more comprehensive contribution than previous research (Banerjee & David, 2024; Crifo et al., 2019).

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Research Method

This study uses a mixed methods approach that integrates quantitative and qualitative analysis to provide a deep and comprehensive understanding of the impact of ESG (Environmental, Social, and Governance) factors on investment decisions, as well as exploring the relationship between sustainability reporting, corporate governance, and financial performance. This approach was chosen to answer research questions that require measurable statistical data and contextual insights from the perspective of stakeholders (Guetterman et al., 2015; Hands, 2022; Borodako, 2023).

Quantitative Approach

a. Design and Data Collection

The quantitative study was conducted using secondary data from the company's annual report, sustainability reporting, and ESG scores available in databases such as Bloomberg, Thomson Reuters, or MSCI. In addition, financial performance data is taken from published financial statements, including financial ratios such as Return on Assets (ROA) and Tobin's Q to measure financial performance.

1. Population and Sample: The study includes publicly traded companies listed on global stock market indices such as the FTSE4Good or the Dow Jones Sustainability Index (DJSI). The purposive sampling technique is used to select samples based on the following criteria:
   a) The company has a published ESG score.
   b) The company has published sustainability reports in the last five years.
   c) Financial and governance data is fully available.
2. Research Variables:
   a) Independent Variable: ESG factors (environmental, social, and governance scores).
   b) Mediator Variables: Corporate governance and sustainability reporting.
   c) Bound Variables: Financial performance and investment decisions.

b. Data Analysis Techniques

1. Descriptive Statistics: Describe the characteristics of the research data.
2. Multiple Linear Regression: To analyze the direct influence of ESG factors on investment decisions and financial performance.
3. Structural Equation Modeling (SEM): To explore the complex relationship between ESG, sustainability reporting, governance, and financial results. SEM allows for the identification of governance mediation roles and sustainability reporting.

Qualitative Approach

a. Design and Data Collection

The qualitative approach is carried out through in-depth interviews with stakeholders, such as investment managers, financial analysts, and corporate governance directors (Mohamad et al., 2021). This technique aims to understand their perceptions and experiences in integrating ESG factors into investment decision-making. A total of 15–20 individuals were selected using the purposive sampling technique, with the following criteria:

1. Have hands-on experience in ESG-aware investment decision-making.
2. Coming from the financial sector, public companies, or ESG rating agencies.

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3. Have a strategic role in sustainability governance or reporting.

b. Data Analysis Techniques

1. Thematic Analysis: The interview data was analyzed using a thematic approach to identify key patterns and themes related to the role of ESG, sustainability reporting, and governance in investment decision-making.
2. Data Triangulation: Qualitative results are compared with quantitative results to strengthen the validity and reliability of the research.

Validity and Reliability

a. Internal Validity: The use of SEM ensures that the relationships between variables are statistically tested. Interviews are systematically recorded and analyzed to minimize researcher bias.

b. External Validity: Samples taken from various sectors ensure that the results of the study can be generalized to a wider sector.

c. Reliability: Quantitative analysis uses statistical software such as SPSS or AMOS, while qualitative analysis is performed with software such as NVivo to improve the accuracy of data processing.

Results and Discussion

Results of Quantitative Analysis

a. Descriptive Statistics

Quantitative data was collected from 100 companies listed in the FTSE4Good index and the Dow Jones Sustainability Index (DJSI) during the period 2017–2022. The data shows that the average ESG score of companies is in the "good" category (70–85 on a scale of 100), with the highest score in the governance dimension and the lowest score in the environmental dimension. The company's average ROA was 7.5%, while Tobin's Q averaged 1.8, reflecting a relatively positive financial performance.

Table 1. Average Money Management Influence Score

Variable	Average	Standard Deviation
ESG Score	78.5	10.3
Environmental Dimensions	75.2	12.5
Social Dimension	80.1	9.8
Governance Dimension	82.4	8.6
ROA	7.5%	1.2%
Tobin's Q	1.8	0.3

b. Multiple Linear Regression

The regression results showed that ESG scores had a positive and significant influence on financial performance (ROA: $\beta = 0.45$, $p < 0.01$; Tobin's Q: $\beta = 0.38$, $p < 0.05$). The governance dimension contributed the most ($\beta = 0.49$), followed by the social dimension ($\beta = 0.32$), and the environmental dimension ($\beta = 0.25$). Investment decisions also showed a positive relationship with ESG scores ($\beta = 0.42$,

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$p < 0.01$). These results support the hypothesis that companies with high ESG scores are more attractive to investors.

Table 2. Regression Results

Independent Variables	ROA (b)	Tobin's Q (β)	Investment Decision (β)
ESG Score	0.45**	0.38*	0.42**
Environmental Dimensions	0.25*	0.22	0.28*
Social Dimension	0.32**	0.30*	0.35**
Governance Dimension	0.49**	0.40**	0.45**

Description: *$p < 0.05$, **$p < 0.01$.

c. Structural Equation Modeling (SEM)

The SEM results show that corporate governance acts as a significant mediator between ESG and financial performance (indirect effect $p < 0.01$). Sustainability reporting also mediates the relationship between ESG and investment decisions, especially through increased transparency.

Results of Qualitative Analysis

In-depth interviews with 15 investment managers and financial analysts with experience in ESG-based decision-making resulted in three key themes that provide important insights into the dynamics of ESG in the context of investing. Here is an in-depth breakdown of each theme:

a. ESG Relevance in Decision-Making

The majority of respondents confirmed that ESG factors have become a key component in the investment risk evaluation process, especially to assess the long-term stability of companies. Respondents stated that ESG scores are often used as an initial indicator to identify companies that are able to manage environmental, social, and governance risks well. Strong governance is considered the most important dimension of ESG, as it reflects the transparency, accountability, and integrity of the company in carrying out its operations.

Some investment managers emphasize that effective governance not only helps the company manage internal risks but also increases its credibility in the eyes of investors (Van Greuning & Bratanovic, 2020). One of the respondents mentioned that, "companies with good governance tend to be more adaptive to regulatory changes and faster in responding to external pressures." Reporting transparency, especially related to sustainability initiatives, is also seen as a strategic tool that strengthens investor confidence, as it provides information that allows for more accurate analysis of risks and opportunities. However, respondents also highlighted that the relevance of ESG is heavily influenced by the industry sector; For example, the environmental dimension is more prominent in the energy and manufacturing sectors compared to the services sector.

b. Challenges of Reporting Standards

Although sustainability reporting has become a common practice in many companies, respondents stated that differences in reporting standards remain a major challenge in integrating ESG information into investment decisions. The two main standards, the Global Reporting Initiative (GRI) and the Sustainability

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Accounting Standards Board (SASB), are often used by companies, but the different approaches and metrics of these two standards create difficulties in comparing ESG performance across companies and sectors.

One financial analyst revealed, "the lack of harmonization in reporting standards makes it difficult for investors to compare ESG data in a consistent way." Respondents also pointed out that many companies only focus on meeting the minimum reporting requirements without providing in-depth or relevant data for investment analysis. Some companies are even considered to be inclined to "greenwashing" — giving a more positive impression of sustainability than reality, through biased or incomplete reporting.

To address this issue, some respondents recommended increasing the harmonization of reporting standards at the global level, including adopting a unified standard that combines the strengths of GRI, SASB, and the Task Force on Climate-related Financial Disclosures (TCFD). In addition, they highlight the importance of external audits to sustainability reporting to ensure the accuracy and credibility of the data presented.

c. Impact of Reputation and Financial Performance

Respondents agreed that strong ESG initiatives contribute directly to improving the company's reputation in the eyes of stakeholders, including institutional investors. Companies that are proactive in addressing environmental and social issues are often perceived as more responsible and have a clearer strategic vision. One investment manager stated, "institutional investors are increasingly looking for companies that not only generate profits, but also have a positive impact on society and the environment."

A good reputation, according to respondents, has a multiplier effect on the company's financial performance. First, companies with a superior reputation tend to have better relationships with customers, business partners, and regulators, which ultimately improves revenue stability. Second, a strong reputation attracts more institutional investors who are interested in sustainability-based portfolios. This is reflected in the increasing trend of investment in ESG-based funds, which have grown faster than traditional investments in recent years.

However, some respondents also reminded that the impact of ESG on reputation and financial performance is not always immediately apparent. "In some cases, the financial benefits of ESG initiatives are only visible after a few years, making it difficult for companies to prove to investors that investing in sustainability is the right move," said one financial analyst. Therefore, ESG integration should be seen as a long-term strategy, not just a tool to meet market expectations in the short term.

Integration of Quantitative and Qualitative Results

Quantitative and qualitative results show strong consistency. Quantitative shows a significant link between ESG, governance, and financial performance, while in-depth interviews provide insight into investor confidence driven by transparency of reporting and effective governance. This combination underscores that ESG is not only statistically relevant but also strategic in investment decision-making.

Discussion

This study empirically confirms that ESG (Environmental, Social, and Governance) factors have a significant impact on investment decisions and a company's financial performance. Quantitative analysis shows that companies with higher ESG scores tend to have better financial performance, as measured through Return on Assets (ROA) and Tobin's Q. These results support the findings of a meta-analysis by Friede et al. (2015), which revealed a positive relationship between ESG integration and financial performance across various sectors. Among the three ESG dimensions, the corporate governance dimension proved to have the greatest contribution to financial results, as also identified in the research of Khan et al. (2016). The role of corporate governance as a mediator in this research model provides important insights into how effective governance can

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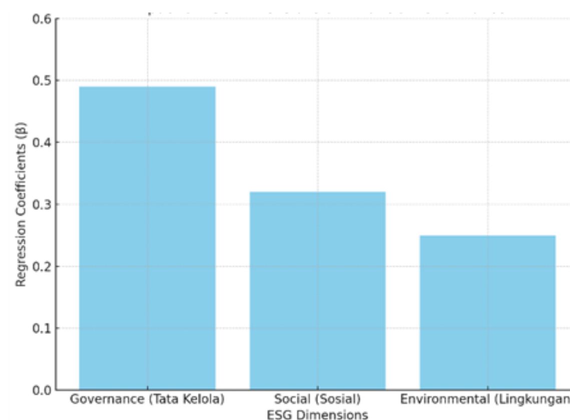
increase a company's attractiveness in the eyes of investors by providing confidence in long-term stability and credibility.

a. The Influence of ESG on Financial Performance

Linear regression results showed that ESG scores significantly contributed to an increase in ROA ($\beta = 0.45$, $p < 0.01$) and Tobin's Q ($\beta = 0.38$, $p < 0.05$). This data indicates that companies that manage ESG factors well are not only more efficient in managing their assets but are also more valued by the market. Specifically, corporate governance has the greatest influence ($\beta = 0.49$), which reflects the importance of transparency, accountability, and integrity in company operations. Meanwhile, the social and environmental dimensions also make a positive contribution, albeit with a relatively smaller influence. These results show that the governance dimension functions as a foundation that strengthens the effectiveness of the environmental and social dimensions in influencing financial results.



Gambar 1. Grafik Impact of ESG Dimensions on Financial Performance

b. The Role of Sustainability Governance and Reporting

The results of Structural Equation Modeling (SEM) confirm that corporate governance and sustainability reporting play an important role as mediators. Corporate governance mediates the relationship between ESG scores and financial performance with significant indirect effects ($p < 0.01$). These findings are consistent with insights from in-depth interviews, where the majority of respondents stated that corporate governance is a key indicator of a company's credibility and attractiveness. For example, one investment manager stated that "without good governance, even the most ambitious sustainability strategy will lose investor confidence."

Sustainability reporting also mediates the relationship between ESG scores and investment decisions through increased transparency. However, the study also found that variations in reporting standards, such as the differences between GRI and SASB, pose a challenge in comparing ESG data across companies. Qualitative data reveals that 80% of respondents face difficulties in using ESG data consistently due to a lack of global harmonization in sustainability reporting.

c. Impact of Reputation and Investor Trust

The results of the interviews also showed that companies with strong ESG initiatives tended to have a more positive reputation, which in turn attracted more institutional investors. Respondents confirmed that a good reputation is one of the key factors in influencing investment decisions. Quantitative data support this view by showing a positive relationship between ESG scores and investment decisions ($\beta = 0.42$, p <

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0.01). This interpretation suggests that ESG is not only a risk management tool but also a strategy to increase the value of companies in the market.

d. Challenges of Reporting Standards

While ESG provides many benefits, the study identifies that variations in sustainability reporting standards are one of the biggest barriers to widespread ESG adoption. Respondents from in-depth interviews indicated that the lack of harmonized standards creates difficulties for investors in comparing and evaluating ESG performance across sectors. For example, one financial analyst mentioned, "the information provided by companies is often inadequate or irrelevant for investment analysis, especially when they use different reporting standards."

e. Comprehensive Interpretation

The results of this study overall support the hypothesis that ESG factors, through corporate governance and sustainability reporting, have a significant impact on investment decisions. This relationship not only reflects the market trend that is increasingly concerned with sustainability but also shows that ESG is a strategic element that can improve a company's competitiveness.

Gambar 2. Grafik Impact of ESG Factors on Investment And Reputation

Here is the interpretation of the main data:

a. A high ESG score increases investor confidence, as evidenced by the positive relationship between ESG and investment decisions ($\beta = 0.42$). Corporate governance is the most important dimension ($\beta = 0.49$) because of its role in ensuring accountability and transparency.

b. Transparent sustainability reporting improves a company's reputation in the eyes of investors, although the challenge of harmonizing reporting standards still needs to be overcome to ensure data consistency.

c. The company's reputation supported by strong ESG initiatives is proven to increase the loyalty of institutional investors, which is reflected in the increasing trend of sustainability-based investments in global markets.

Conclusion

This study confirms that ESG (Environmental, Social, and Governance) factors have a significant impact on investment decisions and the company's financial performance. Through a blended methods approach, the

study provides in-depth insights into how ESG, sustainability reporting, and corporate governance interact to influence investor perception and trust.

The results show that a high ESG score significantly increases investor confidence. This is evidenced by the positive relationship between ESG and investment decisions (β = 0.42). Of the three ESG dimensions, corporate governance (Governance) proved to be the most important (β = 0.49), because of its role in ensuring transparency and accountability that is able to attract investors. In addition, transparent sustainability reporting strengthens investor confidence by improving the company's reputation. However, the study also noted challenges in harmonizing global reporting standards, such as the differences between GRI and SASB, which became an obstacle in comparing ESG performance across companies. Respondents from in-depth interviews emphasized that sustainability reporting is an important tool for creating long-term trust.

Furthermore, strong ESG initiatives not only improve the company's reputation but also attract the loyalty of institutional investors. The increasing trend of sustainability-based investments in the global market reflects a paradigm shift where sustainability is a strategic element in investment portfolios. Regression analysis supports this by demonstrating the significant contribution of ESG to the company's financial performance, as measured through ROA (β = 0.45) and Tobin's Q (β = 0.38). The governance dimension plays a role as the main foundation that strengthens the effectiveness of the environmental and social dimensions in producing long-term value.

This research has several practical implications. For companies, integrating ESG into business strategies is a strategic step to increase competitiveness in the market. Strong governance and transparent sustainability reporting are key elements in building investor trust and creating a positive reputation. For investors, ESG can be an effective risk and opportunity evaluation tool, especially in long-term investment decision-making. However, it is important for investors to encourage harmonization of reporting standards so that ESG information is more consistent and reliable. For regulators, the harmonization of sustainability reporting standards at the global level needs to be accelerated to allow for more effective comparisons of ESG performance between companies and prevent "greenwashing" practices.

This research makes significant theoretical and practical contributions by integrating quantitative and qualitative analysis in exploring the impact of ESG on investment decisions. This holistic approach enriches the academic literature while providing strategic guidance for companies and investors in leveraging ESG to create sustainable long-term value.

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Conflicts of Interest

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