THE ROLE OF BUSINESS STRATEGY IN MODERATING THE EFFECT OF ESG PERFORMANCE ON FIRM VALUE

Areta Xaviera[1*], Annisaa Rahman[2]

Affiliation :

[1,2)]Accounting Program, Faculty of Economics and Business, Andalas University.

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***Correspondence :**
areta26vira@gmail.com

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Abstract

Background: The sustainability issue has become a global conversation both in society and especially in the business world. Climate change, social crises, and environmental issues pose threats to the global economy, especially for developing countries with weaker infrastructures compared to developed nations, thus necessitating sustainable practices, one of which is through ESG disclosure.

Objective: This study aims to empirically examine the influence of ESG performance on firm value with business strategy using Miles & Snow's typology (1978) as a moderator.

Research Methodology: This study uses unbalanced panel data regression with fixed effects using robust standard error to prevent bias in testing the formulated hypotheses. The population in this study consists of non-financial sector companies listed on the Indonesia Stock Exchange (BEI) from 2018 to 2022, with a sample of 194 companies. The data collection method utilizes purposive sampling. Data is analyzed using the panel data regression method.

Research Findings: The results of this study show that ESG performance has a significant negative impact on firm value. Furthermore, this research finds that business strategy can moderate the relationship between ESG performance and firm value, where it strengthens the negative relationship between ESG and firm value. Additional analysis reveals that the defender strategy weakens the negative relationship between ESG and firm value. Meanwhile, the other two strategies are unable to moderate the relationship between ESG and firm value.

Originality/Novelty of Research: This is a study examining the influence of ESG on firm value with business strategy as a moderator in the non-financial sector companies in Indonesia listed on the BEI using data from 2018 to 2022

Keywords: ESG, firm value, business strategy

Introduction

Optimal firm value is the main goal for the company to describe the company's performance to shareholders. Firm value represents the welfare of shareholders which can be seen from an increase in the stock market price (Atan et al., 2018). Based on stakeholder theory, companies also have responsibilities to other stakeholders besides shareholders such as employees, communities, customers and the environment. The existence of social and environmental problems accompanied by global climate change, causing financial performance cannot be the only guarantor of the company's sustainability in the long term, thus requiring disclosure of non-financial performance (Ahmad et al., 2023). Research on non-financial reporting (NFR) practices has rapidly developed over the past decade in several research fields such as business ethics, financial accounting, and strategic management (Turzo et al., 2022). Additionally, Plumlee et.al (2015) showed that components of firm value consisting of equity costs and future cash flows are positively related to NFR. Furthermore, Rezaee & Tuo (2019) provide empirical evidence that the quality of NFR is related to earnings quality. This indicates that stakeholders also require information on non-financial activities as considerations for decision-making in funding companies (Turzo et al., 2022). Environmental, Social, and Governance (ESG) is the most dominant sustainability standard indicator used in current practices to measure companies' non-financial performance (Howard-Grenville, 2021).

According to economic and business research from consulting firm McKinsey, Southeast Asia has the potential to be more severely impacted by climate change compared to other regions in the world(Woetzel et al., 2020). According to the Asian Development Bank (ADB) (2021), developing countries in Asia are the most vulnerable region in the world, including Indonesia. Indonesia ranks 3rd globally in experiencing the most severe climate impacts according to the World Risk Report 2022(Atwii et al., 2022). ADB predicts Indonesia's economy will grow at a rate of 5% in 2024, making it an attractive investment destination in the future. Although Southeast Asia, including Indonesia, experiences strong economic growth, the region still lags behind in sustainable development targets, making ESG performance crucial in this region. This is reinforced by the fact that efforts by countries in this region to develop ESG investments are not balanced with advancements in their economic growth (Pratama et al., 2022).

So far, academics have conducted research on the relationship between ESG performance and firm value(Melinda & Wardhani, 2020) which concludes that investing in high ESG performance promises financial benefits for companies in terms of both value and profitability. In line with Stakeholder theory, companies must also pay attention to stakeholder welfare to achieve company sustainability (Freeman, 1984b). However, these findings are not consistent as other studies have found different results, such as research conducted by Velte (2017) and Yoon et al. (2018) indicating insignificant relationships between ESG-firm value and Behl et al. (2022) finding a negative relationship in the short term. This means that the relationship between ESG and firm value can be influenced by other factors that can strengthen or weaken their relationship. These factors include Business Strategy or Business Orientation. According to Porter (1980), business strategy reflects the actions and choices made by the company in understanding and adapting to the environment and positioning itself in the market to achieve high company performance.

The relevance of business strategy to firm value has been supported by several empirical findings. A study conducted by Waddock & Graves (1997) examined the relationship between Corporate Social Performance (CSP) and financial performance. The study found a positive relationship between CSP and both past and future financial performance. It indicates that companies prioritizing social issues in their strategic decision-making processes experience better financial performance. According to stakeholder theory, companies in dynamic environments face challenges such as changing customer expectations, regulatory changes, employee capacity excesses, and environmental issues, which significantly influence the business strategies adopted by companies (Prahalad & Hamel, 1994). These challenges underlie strategic decision-making, which is a result of the varying expectations of stakeholders (Freeman, 1984a). Anwar & Hasnu (2016) found that business strategies influence financial performance differently. This is due to the uncertainty and instability of the environment and differences in the types of financial performance measures used. Differences in complexity and organizational structure among companies can lead to different challenges in implementing ESG practices that are appropriate to their contexts. Successful ESG implementation requires an approach tailored to the specific characteristics of the company and its organizational structure. Strategies are measured using four constructs following Anwar & Hasnu (2016) which are adaptations of Miles & Snow's (1978) typology. The reason for selecting Miles & Snow's (1978) typology is based on the consideration that this typology is the most cited, criticized, and refined (Anwar & Hasnu, 2016).

This research has two contributions. Firstly, it aims to provide contributions and empirical evidence regarding the influence of ESG performance on firm value. Several studies on ESG and firm value have been predominantly conducted in the regions of developed countries. This serves as a strong rationale for testing due to the differences in characteristics between developed and developing countries. Secondly, this research aims to provide contributions and empirical evidence regarding the role of business strategy in the relationship between ESG performance and firm value. This study expands on the research conducted by Maury (2022) which examined the relationship between CSR, business strategy, and future company performance in companies listed in 23 developed countries by MSCI. This research differs from Maury's (2022) study in its use of the CSR variable. CSR and ESG essentially share the same aspects, which are ways for companies to demonstrate their concern for the impacts of their business activities by focusing on environmental sustainability and social services to society. However, ESG has a broader terminology compared to CSR (Niu et al., 2022). In ESG, governance aspects are directly included, while governance aspects in CSR are indirectly included due to considerations of environmental and social aspects. Therefore, this research intends to test the relationship between ESG and firm value by incorporating the role of business strategy to observe the differences in the influence of each strategy on Indonesian companies.

Literature Review

Agency Theory

Agency theory addresses the principal-agent issue within the context of the separation of ownership and control of the company, which was developed by Jensen, M.C., and Meckling in 1976. This theory elucidates that one of the consequences of agency problems arising in companies is the disclosure of social and environmental responsibilities based on agency theory (Jensen, M. C., & Meckling, 1976). Within the framework of agency theory, companies endeavoring to engage resources for ESG performance are assumed to not allocate their resources productively, which could negatively impact the company's wealth and shareholders' profits. The implementation of ESG practices in companies is also associated with the availability of financial resources. Some critics argue that investments in ESG are considered costly and may lead to agency problems due to significant financial requirements (Xaviera & Rahman, 2023).

Stakeholder Theory

Stakeholder theory, initially developed by Freeman (1984) as a managerial tool, posits that companies are not only responsible for achieving their own objectives but also must consider the well-being of other stakeholders. The ESG disclosure by companies becomes a consideration for stakeholders before they invest their funds. Companies seeking external funding strive to meet the expectations and desires of stakeholders, one of which is sustainability factors. ESG disclosure serves as a means for companies to meet stakeholders' information needs regarding social and environmental responsibilities, reflecting sustainability aspects. This indicates that the corporate management system is not only focused on increasing profitability but also on enhancing the value of ESG obtained through sustainable management applications (Xaviera & Rahman, 2023).

The Influence of ESG on Firm Value

Stakeholder theory states that companies should pay attention to the welfare of their stakeholders and not only focus on their own goals. In achieving stakeholder welfare, companies need to foster good relationships by meeting their expectations, thus gaining support. Companies that want to survive and develop must establish good relationships and get support from stakeholders to increase their company value. One way to gain stakeholder support by meeting their expectations through environmental and social concerns is ESG disclosure, which can ensure the company's long-term reputation leading to an increase in firm value. On the other hand, disclosing social and environmental responsibilities based on agency theory is one of the outcomes of agency problems (Jensen, M. C., & Meckling, 1976). The implementation of ESG in companies depends on the availability of financial resources. Due to financial capability requirements, some critics argue that investing in ESG is costly and leads to agency problems resulting in a decrease in firm value.

So far, academics have researched the relationship between ESG performance and firm value. Sadiq et al. (2020) reported a positive relationship between ESG performance and firm value in meta-analysis. Aydoğmuş et.al (2022) provide empirical evidence that ESG scores are positively and significantly related to firm value. Meanwhile, Wong et.al (2021) examine the impact of ESG certification on firm value, showing that ESG enhances firm value significantly. Other research studies that also found a positive relationship include (Ahmad et al. (2023); Espinosa-Méndez et al. (2023); Rui Cheng et al. (2023); Chang & Lee (2022); Feng & Wu (2021); Thahira & Mita (2021); Melinda & Wardhani (2020); Fatemi et al. (2018). Aboud & Diab (2018)).

H1 : ESG Performance has a positive effect on Firm Value

The Role of Business Strategy in Moderating the Relationship between ESG Performance and Firm Value

According to stakeholder theory, ESG activities represent one way for companies to meet the needs of stakeholders that can be associated with business strategy. Companies operating in dynamic environments face challenges such as changing customer expectations, regulatory changes, employee capacity surpluses, and environmental issues, which significantly influence the business strategies they adopt (Prahalad & Hamel, 1994). The interactions between companies and various stakeholders with differing expectations lead to a convergence of these expectations in the overall corporate social performance (Zamani et al., 2013). Menurut Porter (1980), suggests that business strategy reflects the actions and choices companies make to understand and adapt to their environment, positioning themselves in the market to achieve high performance levels. Bentley et al. (2013) define business strategy as a comprehensive measure related to the complexity and uncertainty of a company's environment, which may not always be present in other company characteristics. Companies prioritizing social and environmental issues in their strategic decision-making process may experience better financial performance and create shared value for all stakeholders. By incorporating ESG considerations into business strategy, organizations can enhance organizational processes, long-term orientation, and measurement and disclosure of non-financial information, which, in turn, can contribute to better performance and value creation (Waddock & Graves (1997); Balian & Ghevondyan (2018); Eccles et al. (2014)).

Miles & Snow (1978) categorize business strategies into three types: prospectors, analyzers, and defenders. Prospectors are characterized by companies continuously seeking to exploit and identify new products and market opportunities through innovation processes, and their competitiveness depends on the company's ability to pioneer products and/or market development. When linked to ESG performance, prospectors are more likely to contribute significantly to ESG performance due to their growth orientation, which necessitates establishing a sustainable reputation and image in the long term. Conversely, defenders focus on narrow and limited product market domains, and their core competencies rely on their ability to enhance production and administrative efficiency. ESG performance is considered not to add cost efficiency, and tends to have high-profit uncertainty, so defenders are less likely to be actively involved in ESG performance. Meanwhile, Analysts take prospective or defensive actions depending on the environmental setting and the balance between efficiency and innovation. Therefore, analyzers are likely to contribute to ESG performance when it is deemed beneficial and vice versa.

Companies that have fully integrated ESG into their business strategy demonstrate better performance in terms of innovation and overall company performance(Bocquet et al., 2017). Servaes & Tamayo (2013) found that CSR and firm value are positively related in companies with high customer awareness, while the relationship is negative or insignificant in other companies. Kong et al. (2020) found that prospector companies take more environmentally friendly actions than defender companies, indicating that business strategy will influence the development of intangible resources such as CSR. Furthermore, CSR investments reflecting ethical responsibility appear to enhance firm value when companies have met their economic responsibilities through competitive efforts (Kim et al., 2018). Maury (2022) tested the relationship between CSR, business strategy, and future corporate performance. Using a sample of companies listed in 23 developed countries by MSCI, CSR implementation was found to be positively related to future financial performance in companies with prospector and growth strategies.

H2 : Business Strategy is able to moderate the effect of ESG performance on firm value

Research Methods

Based on the type of data examined, this research is quantitative in nature. It utilizes secondary data from annual reports listed on the Indonesia Stock Exchange (IDX) for the period 2018-2022, with consideration given to obtaining more recent data during that period. The sampling method employed in this research is purposive sampling, with the following criteria:

Table 1. Sample Selection Criteria

Description	Total
Non-financial public sector company listed on the Indonesia Stock Exchange (IDX) during the period 2018-2022.	4095
Companies that do not have an ESG score issued by Refinitiv Eikon during the period of 2018-2022	(3754)
Companies that do not have complete financial data on Thomson Reuters for the period 2018-2022.	(147)
Total Sample	194

Operational Definition of Variables

Firm Value

The dependent variable in this study is firm value. In this research, firm value is measured by Tobin's Q ratio. The modification of Tobin's Q by Chung & Pruitt (1994) has consistently been utilized in various research simulations and yields an estimate of 99.6% from the original formula used by (Lindenberg & Ross, 1981). Tobin's Q is calculated as follows.

$$Tobin\ 's\ Q = \frac{\text{Total Market Value + Total Book Value of Liabilities}}{Total\ Book\ Value\ of\ asset}$$

ESG Score Performance

The independent variable in this study is the ESG score derived from assessments provided by Refinitiv Eikon. The ESG performance score is an average overall score consisting of assessments in the environmental, social, and governance pillars. These assessments are obtained from information reported by the company to the public. ESG performance is measured using the ESG score from Refinitiv Eikon, designed transparently and objectively to measure the performance, commitment, and relative effectiveness of ESG for companies across 10 key themes (emissions, environmental product innovation, human rights, shareholders, etc.) based on publicly reported data. Environmental performance is measured using the environmental pillar score from Refinitiv Eikon, which consists of three score categories: resource use, emissions, and innovation. Social performance is measured using the social pillar score from Refinitiv Eikon, which consists of four score categories: workforce, human rights, product responsibility, and community. Governance performance is measured using the governance pillar score from Refinitiv Eikon, which consists of three score categories: management, stakeholders, and CSR Strategy.

Business Strategy

The moderation variable in this study is a business strategy using the Miles & Snow (1978) typology. Based on Miles & Snow (1978), business strategies are divided into three groups: prospector, analyzer, and defender. Each variable is measured per company by calculating the rolling five-year average from the beginning of the year. Each calculated variable is ranked into 4 groups (quintiles) each year. The group with the highest quintile will receive a score of 4 (except for the CIR construct which has an inverse measure with the highest score of 0). The second-highest quintile group is given a score of 3 and so on, with the lowest quintile group receiving a score of 0 (except for the CIR construct, which is given a score of 4 for the lowest group). Scores are summed across the four constructs so that company-years can receive a maximum score of 16 and a minimum of 0. The categorization of company strategies will range from scores 0-16 as follows: defender (0-6), analyzer (7-9), and prospector (10-16). Control variables in this study consist of ROA and DAR. The formulation of business strategy measurement calculated with four constructs is presented as follows following Anwar & Hasnu (2016) with the development of the Miles & Snow (1978) typology.

1. MESR (Marketing Expense to Sales Ratio) is a ratio used to measure a company's propensity toward innovation.

$$\text{MESR} = \frac{\text{Marketing Expense (Selling, Administration and General Espense)}}{\mathit{Sales\ Ratio}}$$

2. COGSR (Cost of Goods Sold to Sales Ratio) is a ratio used to determine the focus on product efficiency.

$$\text{COGSR} = \frac{\text{Cost of Goods Sold}}{\mathit{Sales\ Ratio}}$$

3. CASGR (Compound Annual Sales Growth Ratio) is the historical growth rate of a company that measures the strategic growth orientation of the company.

$$\textbf{CASGR}=\left(\frac{\boldsymbol{Ending\ Value}}{\boldsymbol{Beginning\ Value}}\right)^{\left(\frac{1}{\#\ of\ years}\right)} - \mathbf{1}$$

4. CIR (Capital Intensity Ratio) is a ratio used to measure a company's technological focus by dividing total net PPE (Property, Plant, and Equipment) by total assets.

$$\text{CIR} = \frac{\text{Net PPE}}{\mathit{Total\ Aset}}$$

Data Analysis Method

This study uses unbalanced panel data regression to test the hypotheses that have been formulated. Unbalanced panel data is defined as observations of a set of cross-sectional data units over time (time series) with varying numbers of observations each year. The analysis method utilized is panel data regression analysis using the STATA software tool version 17. The regression panel model in this study comprises two models. Research model (1) aims to test hypothesis 1 (H1), which shows the effect of overall ESG performance variables on firm value as shown in equation 1. Research model (2) aims to test hypothesis 2 (H2), which shows the role of business strategy variables in moderating the effect of overall ESG performance on firm value as shown in equation 2.

$$\text{Tobin's }Qit = \alpha it + \beta 1ESGit + \beta 2STRit + \beta 3ROAit + \beta 4DARit + e it \quad (1)$$

$$\text{Tobin's }Qit = \alpha it + \beta 1ESGit + \beta 2STRit + \beta 3ESGit{*}STRit + \beta 4ROAit + \beta 5DARit + e it \quad (2)$$

Description : α = Constant; Tobin's Q = Firm Value; ESG=ESG Performance ; STR = Business Strategy ; ROA = Return On Assets; DAR = Debt to Asset Ratio

Results and Discussion

Result

The study results will first present descriptive statistical data to provide an overview of the data, as seen in the following Table 2.

Table 2. Descriptive Statistical Test Results

	N	Minimum	Maximum	Mean	Std. Deviation
Tobins Q (Y)	194	0.40	8.72	1.5926	1.2079
ESG Score (X)	194	10.18	86.30	48.5210	19.7135
Strategi Bisnis_STR (X)	194	2	13	7.80	2.2784
Leverage_DAR (K)	194	0.11	0.96	0.4753	0.2023
Profitabilitas_ROA (K)	194	-0.18	0.45	0.0780	0.0878
Valid N (listwise)	194				

Source: Stata 17 Output

Table 2 illustrates the descriptive statistics for all variables in this study. Based on the processing results, it is evident that Tobin's Q has a minimum value of 0.40 and a maximum value of 8.72. The firm value measured using Tobin's Q has an average value of 1.5926. This indicates that the value of the researched companies is relatively high, as reflected in the average value greater than 1. It suggests that the market value exceeds the asset value, thus inferring that the market provides a higher evaluation of the company. The standard deviation for this variable is 1.2079.

Furthermore, the ESG scores, as processed from the data in Table 3, have a minimum value of 10.18 and a maximum value of 86.30. The average ESG score obtained from Refinitiv Eikon is 48.5210. This average range falls within the second quartile, indicating relatively satisfactory ESG performance and moderate transparency levels in reporting material ESG data to the public.

The moderating variable, business strategy (STR), has a minimum score of 2 and a maximum score of 3, meaning that the sample in the study consists of companies oriented towards defenders, analyzers, and prospectors. In the sample data of Indonesian companies, there are 51 sample data for prospectors, 64 for defenders, and 82 for analyzers.

Table 2 also shows the descriptive statistics for the control variables, namely ROA and leverage. The maximum value of ROA is 0.45, and the minimum value is -0.18, with an average ROA of 0.078. A higher ROA indicates that a company is more effective in utilizing assets to generate profits. Furthermore, the standard deviation for ROA is 0.087.

The last control variable used in this study is leverage. In Table 2, the maximum leverage value is 0.96, and the minimum value is 0.11, with an average leverage value of 0.4753 for Indonesian companies. High leverage implies that the financing of company assets heavily relies on debt. Additionally, the standard deviation for leverage is 0.2023.

Hypothesis Testing

Based on Table 3, the results of the testing on Model 1 indicate that the ESG score has a coefficient of -0.0095 and a significance value less than 0.05, meaning that the ESG score has a significant negative impact on Tobin's Q. These results demonstrate that H1, which posits that ESG performance has a positive effect on firm value, **is rejected**. Meanwhile, the results of the moderated regression analysis in Model 2 show that the interaction between ESG performance and business strategy has a coefficient of -0.0023 and a significance value less than 0.05, indicating a significant negative effect of the interaction between ESG performance and business strategy on Tobin's Q. Based on the results from Model 1 and Model 2, it is indicated that the business strategy is able to moderate the relationship between ESG performance and firm value. In this study, the corporate life cycle weakens the relationship between the independent variable (ESG performance) along with control variables and the dependent variable (Tobin's Q). These results confirm that H2, which states that business strategy can moderate the effect of ESG performance on firm value, **is accepted**.

Control variables in Model 1 and Model 2 indicate that ROA and Leverage (DAR) do not have a significant impact on Tobin's Q. Furthermore, the coefficient of determination presented in Table 4 shows a determination coefficient of 0.3743 in Model 1, meaning that 37.43% of the independent variable, ESG Score, in this study can explain its dependent variable, firm value, while the remaining 62.57% is explained by variables outside of this study. Additionally, in Model 2, there is an increase in the determination coefficient by 0.3902 when tested with the interaction variable between ESG and business strategy, indicating that 39.02% of the independent variables, ESG, control variables, and the interaction variable between ESG and strategy, can explain the firm value, while the remaining 60.98% is explained by other variables outside of this study.

Table 3. Results of Moderated Regression Analysis.

	Model 1		Model 2	
Variable	Coefficient & Robust Std. Err	Sig	Coefficient & Robust Std. Err	Sig
Constant	2.3198 (0.5424)	0.000	0.9817 (0.5495)	0.074
ESG Score	**-0.0095** (0.0032)	**0.006*** **	0.0139 (0.01068)	0.191
DAR	0.0766 (0.6784)	0.911	0.3569 (0.6569)	0.587
ROA	-0.3700 (0.5801)	0.527	0.3914) (0.7808)	0.616
STR	-0.0349 (0.0248)	0.167	**0.0786** (0.0377)	**0.037** **
ESG*STR			**-0.0023** (0.0010)	**0.031** **
N	194		194	
F Sig	**4.53**	**0.000**	**5.45**	**0.000**
Adj R2		**0.3743**		**0.3902**
*,**,***Signification at 10%, 5% and 1% levels				

Source: SPSS Output

Discussion

The Effect of ESG Performance on Firm Value

Based on the hypothesis testing results, ESG has a significant negative influence on firm value. The findings of this study are consistent with agency theory, which contradicts stakeholder theory. According to agency theory, companies that strive to utilize their resources for ESG performance are assumed not to allocate their resources to more productive costs, which would negatively impact the wealth and profits of shareholders. Advocates of agency costs also argue that companies should perform with the established goal of profit maximization, so resources used for other more productive performances can be allocated (Friedman, 1970). The initial thought regarding ESG was that these are unnecessary costs leading to wealth decline. This perspective aligns with agency theory stating that managers as agents of shareholders tend to spend company resources to gain personal profits (Masulis & Reza, 2015), thus ESG activities will be negatively related to financial performance. Empirically, this agency view is supported by several studies finding a negative relationship between CSR and financial performance. These studies include Bénabou & Tirole (2010); Masulis & Reza (2015) and Krüger (2015). Specifically, Bénabou & Tirole (2010) and Krüger (2015) found evidence consistent with agency theory that managers tend to overinvest in social activities to enhance their personal reputation and lose focus on core managerial responsibilities (Jensen, 2002).

Sonny & Lubis (2023) state that the lack of awareness and knowledge of the public about sustainable investments may contribute to the fact that ESG does not have a significant impact on firm value in Indonesia. Although based on descriptive statistics indicating the average range of ESG scores in companies in Indonesia falls within the second quartile, indicating relatively satisfactory ESG performance and a moderate level of transparency in reporting ESG data to the public, it does not show a positive response from the market. Investors' perception of ESG as a burden may be due to the still minimal regulations regarding ESG in Indonesia. This can be seen from regulations requiring companies to carry out social and environmental responsibility activities. These provisions are regulated in Government Regulation Number 40 of 2007 concerning Social and Environmental Responsibility for Limited Liability Companies. However, these regulations only focus on the social and environmental dimensions, without considering governance issues which are an important element in the ESG framework. Furthermore, regulations related to sustainability reporting in Indonesia only began to be enforced in 2017 through Financial Services Authority Regulation Number 51/OJK.03/2017.

The moderating effect of Business Strategy Moderation on the Relationship between ESG Performance and Firm Value

Based on the results of hypothesis testing, business strategy moderates the impact of ESG on firm value, wherein this effect strengthens the negative influence of ESG on firm value. This implies that the higher the strategy score, the stronger the negative influence of ESG on firm value. In other words, companies that increasingly adopt prospector strategies will strengthen the negative influence of ESG on firm value, while companies that increasingly adopt defender strategies will weaken the negative influence of ESG on firm value. These research findings support stakeholder theory, which emphasizes the importance of building long-term relationships with stakeholders. Long-term relationships can be established through meeting stakeholder demands, including disclosing sustainability performance.

Implementing sustainability performance requires sufficient financial resources, considering that companies engaged in CSR activities often face higher explicit costs and financial expenditures for social projects. Therefore, managerial skills in controlling and managing company costs become crucial. Companies implementing cost leadership strategies, such as defenders, tend to have advantages in asset utilization and resource optimization.

Research indicates that different business strategies can affect financial performance and corporate social responsibility (CSR). For example, prospector strategies are associated with a focus on innovation, risk-taking, and growth, while defender strategies emphasize stability, efficiency, and cost reduction (Widyasari et al. (2017); (Intan et al. (2019)). Prospectors are known as companies that tend to discover new markets, long-term growth, and high innovation, thus carrying high failure risks (Maniora, 2018). From an investor perspective following agency theory, because prospectors incur high costs at the beginning of the year such as research and development costs and marketing costs, the costs incurred for ESG activities can inflate company costs (Friedman, 1970); (Jensen, 2002). These different strategic orientations can lead to different approaches to ESG practices and value creation. It has been found that certain business strategies may prioritize short-term financial gains over long-term sustainability, potentially leading to neglect of ESG considerations for short-term financial gains (Kerr & Monem, 2013). Additionally, the use of certain business strategies, such as earnings smoothing, can lead to financial reporting manipulation, which can obscure a company's true ESG performance (Intan et al., 2019). In short, business strategy choices based on Miles & Snow typology can have significant implications for a company's approach to ESG practices and overall value. Different strategies may prioritize financial performance, tax planning, and short-term gains over long-term sustainability and ESG considerations, potentially weakening the relationship between ESG and firm value.

Expansion Test

The Expansion Test is necessary within the context of testing the moderation of each business strategy, namely prospector, defender, and analyzer, on the relationship between ESG (Environmental, Social, and Governance) and firm value. Each business strategy may have different impacts on the relationship between ESG and firm value. The Expansion Test helps identify this variability and provides deeper insights into the contribution of each strategy. Furthermore, each business strategy may have a different approach to ESG practices. Additional analysis can help identify whether there is a differentiation in ESG impact depending on the adopted business strategy. By conducting this expansion test, research can provide a more holistic and in-depth contribution to understanding how business strategies can moderate the relationship between ESG and firm value.

Table 4. Additional Test Results

	Defender		Analyzer		Prospector	
Variable	B	Sig	B	Sig	B	Sig
Constant	2.1557	0,000	1,9797	0,000	2,0514	0,000
ESG_Score	-0.0122	0,001	-0.0074	0,075	-0.0087	0,008
DAR	0.0597	0,931	0.0528	0,941	0.0505	0,941
ROA	-0.5173	0,371	-0.5823	0,304	-0.6186	0,298
DEF	-0.4427	0,057				
ANZ			0.2312	0,191		
PROS					0,0195	0,903
Moderation Effect						
ESG*Defender	0,0120	**0,061***				
ESG*Analizer			0,009	**0,239**		
ESG*Prospector					-0,0012	**0,682**
N	194		194		194	

*,**,***Signification at 10%, 5% and 1% levels
Robust Standard Error

Source: Stata 17 Output

The effect of ESG Performance on Firm value in Defender Strategy

The findings of this study reveal that the interaction between ESG performance and defender business strategy yields a coefficient value of 0.0120 with a significance level of 10%, indicating a positive impact of ESG performance and defender strategy on firm value. In other words, companies oriented towards the defender strategy are likely to weaken the negative impact of ESG on their firm value. This suggests that defender-oriented companies may have internal mechanisms or practices that help mitigate the negative effects of ESG on their firm value. However, it is important to note that these findings are descriptive and limited to a sample of companies in Indonesia.

Nollet et al. (2016) emphasize that Corporate Social Responsibility (CSR) strategies may have nonlinear and selective effects on financial performance, suggesting that defender companies, by adopting a more conservative approach and risk avoidance, may be better positioned to integrate ESG activities into their operations, thus maximizing their financial performance. Additionally, Atan et al. (2018) note that previous studies have found a positive relationship between sustainability and firm value, implying that defender companies, with their emphasis on risk reduction and operational efficiency, may be more effective in leveraging ESG factors to enhance their overall performance and value. Studies by (Gao et al., 2008) provide evidence that defender strategies have a positive impact on returns within 30 days, supporting the notion that defender strategies can contribute to profitable company performance. These findings suggest that companies employing defender strategies may experience short-term performance improvements, possibly due to the protective nature of these strategies in volatile market conditions, leading them to be cautious in integrating ESG activities into their operations considering costs to maximize their financial performance.

The Effect of ESG Performance on Firm Value in Analyzer Strategy

The results of this study indicate that the interaction between ESG performance and defender business strategy does not significantly affect firm value. Eccles et al. (2014) found that companies with high sustainability levels tend to have established processes for engaging stakeholders, are more long-term oriented, and demonstrate higher levels of non-financial information measurement and disclosure. This suggests that the impact of ESG on firm value may be more related to sustainability practices and stakeholder engagement. In unstable business environments, analyzers tend to observe their competitors' activities in making business strategy decisions. Hughes & Morgan (2008) explain that this observation requires learning, and they highly value market information. Strong learning will support success in pursuing profit as a secondary driver. According to Yuan et al. (2020), analyzers will depend on the environmental setting and balance cost efficiency and product differentiation in deciding whether to take prospective or defensive actions. Previous research indicates that analyzers are led by managers with diverse backgrounds including marketing, production, engineering, and finance (Miles & Snow 1978, 2003). With the various backgrounds of the management team, conflicts may arise, thus inhibiting decision-making (Galbreath, 2010). Therefore, there is little likelihood that these companies can maximize environmental social responsibility performance, resulting in suboptimal ESG actions.

The Effect of ESG Performance on Firm Value in Prospector Strategy

The results of this study indicate that the interaction between ESG performance and prospector business strategy does not significantly affect firm value. Higgins et al. (2015) highlight that prospectors quickly transform their product market mix into innovative market leaders in various fields, while defenders maintain a narrow and stable product focus to compete based on price, service, or quality. Continuous changes and innovations by prospector companies may lead to a lack of stability and consistency in their ESG practices, potentially hindering the formation of strong relationships between ESG and firm value. Furthermore, Bentley-Goode et al. (2019) note that the success of prospectors depends on aggressive marketing efforts, while the success of defenders depends on improving operational efficiency. Emphasis on aggressive marketing may lead to a focus on short-term profits and market position rather than long-term sustainability and holistic integration of ESG considerations, which are crucial for enhancing firm value. Moreover, Arianwuri et al. (2017) found that prospector business strategies have a positive influence on the risk of stock price decline, indicating a potential tendency towards higher risk-taking behavior. This risk orientation may lead to prioritizing financial performance over ESG considerations, thus limiting prospectors' ability to effectively moderate the relationship between ESG and firm value. In conclusion, prospector company strategies may not effectively moderate the relationship between ESG and firm value due to their focus on innovation and aggressive marketing, which may result in instability in ESG practices and potential prioritization of short-term financial gains over long-term sustainability.

Conclusion

Based on the results of hypothesis testing conducted, it can be concluded that ESG performance has a significant negative impact on firm value, and business strategy is capable of moderating the influence of ESG on the value of non-financial sector companies listed on the IDX for the period 2018-2022. This is because investors in Indonesia continue to perceive ESG implementation and reporting as costs that reduce company profitability and because there are no strict regulations regarding ESG implementation and reporting. This conclusion is consistent with agency theory, which states that ESG activities will create agency problems between company managers and agencies. Additionally, there is a difference in awareness where developed countries have a higher level of societal awareness in demanding companies to be environmentally responsible compared to developing countries like Indonesia.

In this study, business strategy is capable of moderating the influence of ESG performance on firm value. Defenders were found to weaken the negative relationship between ESG performance and firm value, representing that defender companies, known for their focus on stability and efficiency, may be more inclined to provide high-quality ESG information, thereby enhancing their firm value. Defender companies, by adopting a more conservative approach and avoiding risks, maybe in a better position to integrate ESG activities into their company, thus maximizing their financial performance. For prospector strategies, ESG performance tends to be insignificant to firm value, representing companies whose focus is on innovation and aggressive marketing as well as high-risk-taking, which may lead to a lack of stability in ESG practices and potential short-term financial profit priorities over long-term sustainability. On the other hand, this could also mean that companies incorporating ESG into their business strategy do not receive a positive response from investors, thus not impacting the increase in firm value. For analyzer strategies, ESG performance tends to be insignificant to firm value, representing companies in unstable business environments, analyzers tend to monitor their competitors' activities in making business strategy decisions. Thus, there is a small chance these companies can maximize environmental and social responsibility performance, resulting in suboptimal ESG actions.

It is hoped that the results of this study will assist the government in strengthening environmental and social responsibility disclosure laws with clear and strict sanctions. This will encourage companies to participate in environmental responsibility performance and sustainability reporting. The implications of this research also provide input for companies by identifying concrete steps that can be taken by companies in integrating ESG into their business strategies. Companies can enhance engagement with stakeholders, including customers, employees, and investors, to better understand their expectations regarding ESG practices. This allows companies to align their business strategies with stakeholder needs and values. Therefore, detailed guidelines or implementation strategies should be developed to demonstrate how companies can integrate ESG aspects into their business strategies. This may include developing sustainable performance measurement methods, implementing concrete initiatives to reduce environmental impact, and forming internal teams responsible for reporting and implementing sustainability policies. Thus, the implications of this research can provide clear and practical guidance for companies in adopting and integrating sustainability practices into their corporate structure and operations to optimize their positive impact on firm value.

This study is not without limitations, namely the subjectivity in measuring companies' ESG disclosures. This study excludes financial companies from the research sample, assuming that this industry has significantly different regulations compared to other industries. Therefore, future research could examine companies, especially in the financial industry, to see how sustainability performance achieved by companies is achieved through business strategies. Additionally, the findings of this research regarding company compliance with ESG performance disclosures cannot be generalized because ESG disclosure regulations are still voluntary in Indonesia. Since the focus of this research is only on companies in Indonesia, the results cannot be generalized to other developing countries. Additional variables that can explain the correlation between ESG performance and firm value (such as financial resources, inter-industry characteristics, earnings management, etc.) are expected to be used in future research.

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