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Evaluation of the Relationship between Environmental, Social & Governance (ESG) Implementation and Company Efficiency: A Study on Sri-Kehati Index

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A R T I C L E I N F O

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ABSTRACT

This study aims to investigate the effect of Environmental, Social, and Governance (ESG) scores on firm performance. Corporate performance is measured through the ratio of total asset turnover. The data used is historical annual data for 5 years from companies listed in the Sri-Kehati index. The method used in this research is regression analysis with a quantitative approach, where secondary data for the 2019-2023 period is obtained from various databases such as Refinitiv Eikon, RTI Business, Sustainalytics, and MSCI ESG Ratings. The results show that there is a negative relationship between ESG scores and total asset turnover, indicating that an increase in ESG scores correlates with a decrease in efficiency in the utilization of company assets.

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1. INTRODUCTION

The increasing awareness of the public regarding the company's impact on the environment and social means that companies must strive to minimize their negative impact on the environment and society. Companies will also ensure that they operate fairly and transparently. There are many reasons why corporate social responsibility and ethics are important. Firstly, it can help companies to improve their reputation. Companies that have a good reputation will find it easier to attract customers and employees. Second, social responsibility and ethics can help companies reduce risks. Companies that operate ethically are less likely to be involved in scandals or face lawsuits. Third, social responsibility and ethics can help companies improve financial performance. Companies that invest in social and environmental programs often see improvements in profitability and productivity.

Researchers found the problem that there are still many companies that have a TAT score below 1, which indicates that the company generates less revenue than the industry average, the company may not use its assets efficiently. There is a possibility that the company has problems in its business strategy. Tommaso & Thornton, (2020) investigated the relationship between European banks' ESG scores and risk-taking behavior. The authors concluded there was a positive correlation between high ESG scores and reduced risk-taking behavior. Reduced risk-taking behavior results in a “diversion of scarce resources away from investments,” which means a decline in financial performance. Atan et al., (2018) conducted research with data from Malaysian public limited companies. The aim of this research is to investigate the relationship between how well companies address ESG factors and company performance due to increasing concerns among investors, creditors, and governments. The authors conclude that there is no significant relationship between ESG factors and company profitability nor between ESG and company value. Ruan & Liu, (2021) investigated China's capital markets, focusing on the relationship between ESG and corporate performance. The results show a significant negative

correlation between ESG activities and company performance, where increased costs due to ESG activities appear to be the main reason for this correlation.

In short, the relationship between ESG and company performance is unclear as there are different studies with different results. There is research that supports a significant positive relationship between ESG and company performance, while several other studies support a significantly negative relationship. Several studies also support a non-significant relationship between ESG scores and company performance. Therefore, researchers want to examine this matter again with differences in terms of countries, companies and financial performance methods that use total asset turnover.

Sustainability is a term or concept that has several different meanings for researchers and people in general (Ramsey, 2015). Moore et al., (2017) argue that sustainability faces challenges. Among them is the lack of a standard and widely accepted definition. Baumgärtner & Quaas, (2010) argue that "Sustainability is a normative idea about the way humans should act towards nature, and how they are responsible towards each other and future generations". In the economic field, sustainability is related to sustainable financing, which refers to the question of whether loans that have been given will be repaid, and corporate sustainability, which refers to the company's success in the long term (Ben-Eli, 2018). Bateh et al., (2013) put forward a similar argument and stated that in business, sustainability can be defined as "longevity, maintenance of core principles or goals, and responsibility for external needs". From a broader perspective, the term sustainability is used in the context of our planet as a whole. This refers to the health and integrity of all its inhabitants, including animals, forests, oceans, and the future well-being of humanity (Ben-Eli, 2018). The main message that can be learned from the author is the long-term health and well-being of the world and its people. Regarding business and economics, the main message is responsible business practices and long-term thinking for both internal and external aspects of business.

Friedman, (1970) first put forward the Shareholder theory in 1970. This theory states that the only obligation of a company is to maximize profits to satisfy its shareholders. If a company is a collection of contracts, then no one owns it. One person cannot have problems that can arise due to stakeholder involvement in activities if the only reason is because that is what is expected of them. In this case, this can lead to increased costs, decreased revenues, and investment in projects with low returns, which otherwise might be rejected. Furthermore, it is stated that if shareholder money is spent for the benefit of society, then this is wasteful expenditure, because the money could be used to develop the business. Additionally, shareholders have the ability to spend their own money on certain activities if they wish to do so. So, there is no point in doing it on behalf of shareholders. Basically, businesses should not spend money on social causes unless the shareholders themselves would spend the money in the same way because businesses must always act in the best interests of their shareholders. (Friedman, 1970). The focus on shareholder interests is justified for several reasons. First, when discussing shareholder property rights, do they own the company's property? If they are viewed as owners, their property interests must be protected. Second, in line with the fact that directors have an agency relationship with shareholders, company boards and directors are expected to pursue the best interests of clients. Public policy states that “institutions in which management is primarily responsible to shareholders provide the most socially beneficial system of economic organization”, meaning that companies must act in the best interests of their shareholders because they provide benefits to all constituents (Moore et al., 2017).

The main interest of shareholders is the success of the company. Like any investor, they want their investment to be good and profitable. We believe that this theory can be useful in understanding parts of our results depending on the outcome. Suppose the results show a negative relationship between ESG scores and profits, as well as between ESG and stock returns. In this case, this theory suggests that companies should not pursue high ESG scores because it will be detrimental to the company's shareholders. According to the efficient market hypothesis (EMH), securities markets are efficient, and all available information is reflected in security prices. Information flows smoothly and is incorporated into the stock market without interruption or delay (Fama, 1970). Market efficiency is often divided into three levels or forms: weak, semi, and strong. In weak form, current stock prices reflect historical information such as past prices and trading volume. Here, information advantages can be used to generate abnormal profits. Current stock prices reflect past and present public data in semi-strong form. In this case, unequal access to information or the timing of data availability may provide an advantage to some investors if they act on the data before the market. In strong form, stock prices reflect all available data, whether public or not. Here, one cannot outperform the market because all available

data is factored in shares. Therefore, there will be no information asymmetry because everyone has access to all information at all times, and no one has access to more information than anyone else (Degutis & Novickytė, 2014).

Since this theory was recognized and defined, it has received a lot of attention over the years. The validity of this theory has been questioned over time. Some experts argue that there is no more valid hypothesis than the EMH. Others argue that the supply of information does not fully reflect prices. EMH faces two types of problems: theoretical inconsistencies and other problems lying in market anomalies. The first problem lies in market efficiency. If everyone believes that the market is efficient, then the market will no longer be efficient. Anomalies are deviations from accepted paradigms. In the case of the EMH, various anomalies have emerged over time, but have a limited time span in the financial literature (Leković, 2018).

2. RESEARCH METHOD

This research uses a quantitative approach method. This method functions to understand whether there is an ESG influence on Total Asset Turnover in companies included in the 2019-2023 Sri-Kehati Index by processing the data that has been obtained (secondary data) using the SPSS version 25 statistical tool. The research test used is analysis multiple linear statistics. The population in this research is all companies listed on the Indonesian Stock Exchange using purposive sampling, where companies that are active in financial reporting, have ESG scores and are included in the Sri-Kehati index. The population of this research was 25 companies from which 13 samples were then taken after using a purposive sampling technique. The data collected was 65 data. In this research, researchers obtained data from various sources which is secondary data. The method taken is library documentation, which is considered a good data collection technique for secondary data taken from companies.

3. RESULTS AND DISCUSSIONS

Table 1. Descriptive Statistical Test Results

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Total_Asset_Turnover	65	.45	1.25	.6917	.20231
Environment	65	66.00	94.00	82.3846	6.29408
Social	65	76.00	95.00	86.1538	4.21764
Government	65	78.00	97.00	88.2308	4.26017
Valid N (listwise)	65				

Based on table 1, it can be seen that there is a dependent variable, namely Total Asset Turnover and 3 (three) independent variables, namely environment, social and government with 65 research data obtained in the period 2019 to 2023. The calculation results during the observation period show that, Score total asset turnover (TATO) in financial reports shows how efficiently the company uses its assets to generate sales. This score is calculated by dividing total sales by the company's average total assets during a certain period. The highest Total Asset Turnover score is owned by PT Unilever Indonesia Tbk (UNVR) in 2023. This shows that PT Unilever Indonesia Tbk (UNVR) in 2023 will be efficient in using its assets. The Total Asset Turnover value is owned by PT Adaro Energy Tbk (ADRO) with a score of 0.45. This figure shows that ADRO is less efficient in using its assets. The mining industry, such as coal which ADRO is involved in, generally has a lower Total Asset Turnover than other industries. This is because this industry requires large fixed assets, such as mines, equipment and infrastructure, to generate sales. The average score for Total Asset Turnover is 0.69, which means that the average company is still not efficient and uses its assets to generate good sales. The standard deviation of 0.202 in the environmental score shows how wide the environmental score values are around the average. In this context, a value of 0.202 indicates that the environment score value is concentrated around the average. Most companies have environmental scores that are not much different from the average and the variability of environmental scores is relatively low. No company has a very high or very low environmental score.

A high Environment score shows that the company has done a lot to protect the environment. Companies with high Environment scores can attract investors who care about environmental sustainability and improve the company's reputation. The lowest score for Environment is PT Adaro

Energy Tbk (ADRO) with a score of 66. This is because the company has a high risk of being impacted by environmental regulations, such as fines or sanctions. The highest score was achieved by PT Unilever Indonesia Tbk (UNVR) with a score of 94. This shows that PT Unilever Indonesia Tbk (UNVR) has good environmental performance such as responsible waste management. The average Environment score is 82.3, meaning that the majority of companies have good environmental performance. This shows that these companies have made efforts to manage the impact of their operations on the environment. The standard deviation shows the number 6.29408, meaning there is a significant difference between the environmental scores of various companies. This shows that some companies have environmental performance that is much better or much worse than the average.

Companies with high social scores have a good reputation as companies that are responsible and care about society. The highest social score is owned by PT Unilever Indonesia Tbk (UNVR), which shows that this company has good social programs for the community. PT Unilever has several programs from a social perspective, namely healthy and prosperous programs such as lifeboy healthy sharing, clean sunlight, the Unilever partnership program and the Unilever program for small traders. The smallest score, namely 76, is held by PT Adaro Energy Tbk (ADRO). This happens because Adaro is a coal company, and coal is a significant source of greenhouse gas emissions. Greenhouse gas emissions contribute to climate change, which has negative impacts on society and the environment.

A good Government score shows that the Company complies with applicable regulations, including regulations related to the environment, social and governance. This can increase investor and public confidence in the company. The highest score from Government is owned by PT Unilever Indonesia Tbk (UNVR) with a score of 97. This figure shows that PT Unilever is a company that complies with regulations and the company has effective risk management, which is demonstrated by proper risk identification, assessment and mitigation. . The lowest score was owned by PT ADRO with a score of 78.

Table 2.
Regression Test Results

Coefficientsa

Model		Unstandardized Coefficients	
		B	Std. Error
1	(Constant)	,730	,783
	Environment	,029	.016
	Social	-.011	,048
	Government	-.001	,040

a. Dependent Variable: Total_Asset_Turnover

Based on the test results in table 5.5. Then you can find out the coefficient value of each variable and its level of significance. The coefficient values that have been obtained are in table 5.5. can be broken down into a multiple regression equation. From the multiple linear regression equation above, it can be explained that, the constant value (a) shows a positive value of 0.730. A positive sign means that it shows a unidirectional influence between the independent variable and the dependent variable. This shows that if all the independent variables which include Environment (X1), Social (X2), and Government (X3) have a value of 0 or have not changed, then the share price value is 0.730. The regression coefficient value for the Environment variable (X1) is 0.29, indicating a positive influence between Environment and Total Asset Turnover. This means that if the Environment variable increases by 1 time, then on the other hand the share price variable will increase by 0.029 assuming that the other variables remain constant. The regression coefficient value for the Social variable (X2) is -0.11 indicating a negative influence between the Social variable and Total Asset Turnover. This means that if the Social variable increases by 1 time, then the Total Asset Turnover variable will decrease by -0.11 with the assumption that the other variables are constant. The regression coefficient value for the Government variable (X3) has a negative value of -0.001. This shows a positive influence if Government experiences an increase of 1 time, then Total Asset Turnover will also decrease by -0.001 with the assumption that other independent variables are considered constant.

The coefficient of determination is used to measure the level of strength of the relationship that exists between the independent variable and the dependent variable and can explain how much the independent variables together can explain the dependent variable. The following are the results of the coefficient of determination test.

Table 3.
Determination Coefficient Test Results

Model summary				
Model	R	R square	Adjusted r square	Std. Error of the estimate
1	.676a	,456	,430	.15279

A. Predictors: (constant), government, environment, social

Based on the regression results in table 4.8 above, it can be seen that the Adjusted R square value is 0.456 or 55.6%. So it can be concluded that the variables namely Environment, Social and Government influence Total Asset Turnover by 46.5%, while the remaining 54.5% is influenced by other variables not examined in this research.

4. CONCLUSION

Based on the results of research and discussion regarding the influence of Environmental, Social, and Governance (ESG) aspects on total asset turnover in companies incorporated in the Sri-Kehati Index during the period 2019 to 2023, it can be concluded that these three aspects do not show a significant influence on the efficiency of the use of company assets. Specifically, the environmental aspect is not statistically proven to affect the level of asset turnover. This indicates that the company's various initiatives in preserving the environment, such as waste management, energy efficiency, or carbon emission policies, have not had a real impact on the operational effectiveness of their assets. Similarly, social aspects, which include corporate social responsibility, protection of employee rights, and relationships with communities and consumers, also do not have a significant effect on total asset turnover. This suggests that corporate social efforts have not directly improved asset efficiency performance. Meanwhile, aspects of corporate governance, which include the structure of the board of directors, transparency, and compliance with regulations, also do not contribute significantly to the efficiency of asset management. Thus, the implementation of good corporate governance principles in the companies in this index has not shown concrete results on operational efficiency. Based on the results of research and discussion regarding the influence of Environment, Social and Government on Total Asset Turnover included in the Sri-Kehati index during 2019-2023, the following conclusion can be obtained: Environment does not have a significant influence on Total Asset Turnover in companies included in Sri-Kehati Index. Social does not have a significant influence on Total Asset Turnover in companies included in the Sri-Kehati Index. Government does not have a significant influence on Total Asset Turnover in companies included in the Sri-Kehati Index

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