



Corporate Governance And Market-Based Value In ESG-Adopted Firms: The Moderating Role Of Institutional Ownership

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ABSTRACT

This study investigates the relationship between corporate governance and market-based firm value in ESG-adopted firms listed on the Indonesia Stock Exchange between 2019 and 2023, and examines the moderating role of institutional ownership. The analysis employs panel data regression with a sample of 161 companies, using variables measured by Tobin's Q, Bloomberg Governance Performance Score, and institutional ownership percentage. The results indicate that corporate governance has a significant positive effect on firm value. Control variables reveal that growth and profitability positively influence firm value, while leverage and firm size have negative effects. However, institutional ownership does not significantly moderate the governance-value relationship. The findings highlight that robust governance practices play a crucial role in enhancing firm value in ESG-adopted Indonesian companies, regardless of institutional monitoring mechanisms.

INTRODUCTION

The optimization of firm value has become a growing focus in contemporary business, with corporate governance increasingly examined as a critical factor influencing market valuation, particularly in firms adopting Environmental, Social, and Governance (ESG) principles (Yu & Xiao, 2022). High firm value enhances capital market access and reduces funding costs (Duan et al., 2023), while strong corporate governance signals effective risk management and future value creation potential (Nguyen et al., 2022).

However, when firm value is compromised due to governance failures, companies face increased capital costs and declining investor confidence that can hinder business growth (Bui & Krajcsák, 2023). Corporate governance scandals have substantially impacted firm value through market reactions and regulatory penalties. The Wirecard case demonstrated severe value implications, with the stock price plummeting 98.8% from €104.50 to €1.28 in June 2020 and €12.4 billion in market value destroyed following the revelation of €1.9 billion in missing funds

and subsequent governance failure (Jo et al., 2021). These cases emphasize the growing importance of corporate governance in market valuations, especially within ESG-adopted firms.

Research examining corporate governance's impact on firm value shows mixed results. Studies by (Seok et al., 2024a) and (Tang et al., 2024a) document positive effects. Conversely, other studies, such as those by (Duque-Grisales & Aguilera-Caracuel, 2021) and (Y. Christiawan et al., 2024) identify negative impacts. Meanwhile, research by (Faure et al., 2025a) and (An et al., 2024) find no significant impact. These divergent findings may be due to moderation variables not being considered in depth in previous studies (Baron & Kenny, 1986).

(Thruong, 2024) suggested that future research should consider institutional ownership as a moderating variable, as this type of ownership may play a crucial role in governance effectiveness through sophisticated monitoring and influence mechanisms. Institutional investors possess the resources and expertise to effectively monitor management actions and corporate governance practices. Their sophisticated monitoring capabilities and long-term investment horizons make them particularly well-positioned to influence corporate governance mechanisms and potentially enhance their impact on firm value.

This research examines whether institutional ownership moderates the impact of corporate governance on market-based firm value in ESG-adopted Indonesian listed companies from 2019 to 2023. Institutional ownership is posited to enhance the positive impact of corporate governance through sophisticated monitoring of governance performance, expertise in evaluating governance structures, and influence over management decisions. By focusing specifically on ESG-adopted firms, this study addresses a significant context where governance mechanisms are particularly relevant due to the explicit commitment to environmental, social, and governance principles.

The Indonesian market provides a unique research setting due to its emerging market characteristics and ongoing corporate governance reforms. Indonesia has implemented various corporate governance initiatives and regulations in recent years, making it an interesting context to examine how institutional ownership influences the effectiveness of these governance mechanisms. Furthermore, the growing adoption of ESG principles by Indonesian listed companies creates an opportunity to investigate how institutional ownership affects the relationship between corporate governance and firm value in this specific context.

This study's novelty lies in examining institutional ownership's moderating role in the corporate governance-firm value relationship, specifically within ESG-adopted firms in the Indonesian market context. Previous studies have primarily focused on direct relationships or different moderating variables, leaving a gap in understanding how institutional ownership affects this relationship in firms that have explicitly adopted ESG frameworks. This research contributes to academic literature and practical understanding of how institutional ownership can positively moderate the impact of corporate governance on market-based firm value.

Signaling theory, first introduced by (Spence, 1973) in his research on the labor market and education, it was later developed in the financial context by (Ross, 1977), who explained how companies provide signals to users of financial statements. Signaling theory posits that high-quality companies intentionally send signals to the market, allowing it to distinguish between excellent and low-quality companies (Morris, 1987). In corporate governance and firm value, signaling theory suggests that companies with robust governance mechanisms will communicate this as a positive signal to investors and stakeholders. This indicates the company's focus on long-term performance (Kong et al., 2020). Disclosure of good governance practices can be a credible signal, as companies with poor governance would find it difficult to imitate such practices (Zhou et al., 2021).

Agency theory discusses the relationship between principals (shareholders) and agents (management) that arises from the separation of ownership and control (Jensen & Meckling, 1976). The theory suggests that information asymmetry and conflicting interests between principals and agents can lead to agency problems. When neither party receives maximum

benefits, conflicts of interest occur. Managers have dual responsibilities of maximizing owners' earnings and pursuing personal interests. According to (Jo et al., 2021), management's actions regarding governance practices may not always align with shareholders' interests, as managers might focus on short-term performance over long-term governance investments. Corporate governance mechanisms are designed to mitigate these agency problems by aligning management's interests with those of shareholders and ensuring transparency and accountability.

Market-based firm value represents market participants' assessment of a company's worth, commonly measured using the Tobin's Q ratio (Faure et al., 2025b) (Y. J. Christiawan et al., 2024) (Seok et al., 2024b) (Tang et al., 2024a) (An et al., 2025). This measure compares a company's market value to its asset replacement cost, providing insights into market perceptions of its future growth prospects and performance. According to (Duan et al., 2023), higher firm value enhances access to capital markets and reduces funding costs, making it a crucial metric for business sustainability.

Corporate governance in ESG-adopted firms encompasses the structures and processes by which companies are directed and controlled, with a particular emphasis on ethical standards, transparency, and accountability within the broader ESG framework. Good governance can enhance a company's reputation, reduce regulatory risks, and improve operational efficiency (Buchetti et al., 2025). Several studies have found a positive impact of corporate governance on firm value, particularly in ESG-conscious organizations (Tang et al., 2024a) [22].

The impact of corporate governance on market-based firm value in ESG-adopted firms can be explained through multiple mechanisms based on signaling theory. When companies demonstrate solid governance practices, they signal effective management capability (Faure et al., 2025a). Such signals can enhance corporate reputation, reduce regulatory risks, and improve stakeholder relationships (Seok et al., 2024a). Furthermore, superior governance indicates the company's ability to effectively manage complex challenges and future risks (Buchetti et al., 2025). Based on these theoretical arguments and empirical evidence, this study proposes:

H1: Corporate governance has a positive impact on market-based firm value in ESG-adopted firms.

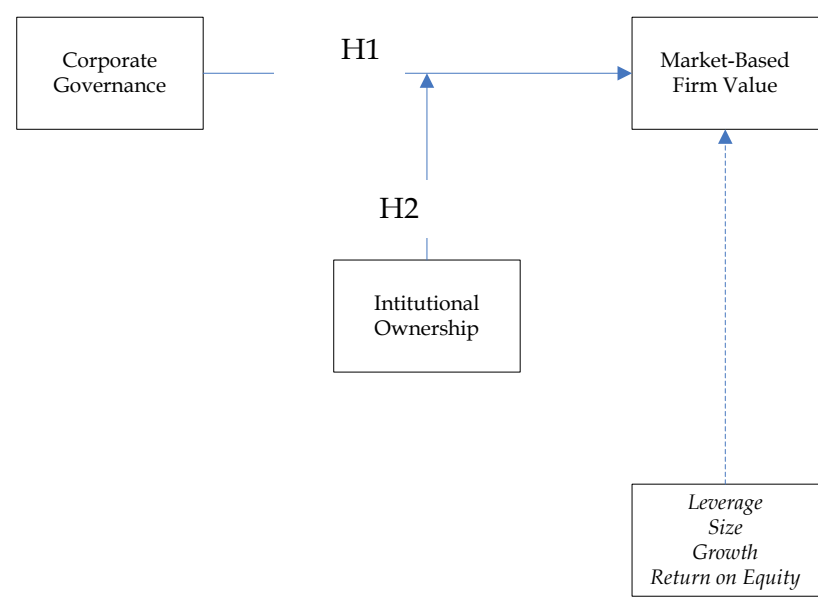
Institutional ownership reflects shareholdings by professional investment entities such as mutual funds, pension funds, and insurance companies. These sophisticated investors typically employ comprehensive monitoring mechanisms and often pressure companies to adopt governance best practices. Their long-term investment horizons and access to governance expertise allow them to evaluate and impact companies' governance strategies effectively. (Solarino & Boyd, 2020) state institutional owners can significantly impact corporate governance practices through voting power and management engagement. Hartzell and Starks (2003) suggest that institutional ownership provides a crucial external monitoring mechanism for enhancing governance mechanisms and creating firm value.

The moderating effect of institutional ownership on the relationship between corporate governance and market-based firm value can be understood through agency theory. Institutional ownership enhances the effectiveness of corporate governance through sophisticated monitoring and pressure for best practices. According to agency theory, institutional owners serve as external monitors who can reduce agency costs and improve governance implementation (Hartzell & Starks, 2003). Their presence signals effective oversight of governance structures and increases the credibility of governance mechanisms (Sakawa, 2020). Institutional investors' expertise in evaluating governance practices can lead to more effective implementation of governance strategies (Velte, 2024). Based on these arguments, this study proposes:

H2: Institutional ownership positively moderates the relationship between corporate governance and market-based firm value in ESG-adopted firms. Consequently, the relationship between

corporate governance and market-based firm value becomes stronger when the level of institutional ownership is high.

Figure 1. Conceptual Framework



Source: Research Data, 2025.

LITERATURE REVIEW

Corporate Governance and Firm Value

Corporate governance refers to the mechanisms, processes, and relations by which corporations are controlled and directed. It plays a crucial role in ensuring accountability and transparency, especially in firms committed to Environmental, Social, and Governance (ESG) principles. Several empirical studies have shown that strong governance mechanisms contribute positively to firm performance and valuation. For instance, Seok et al. (2024) and Tang et al. (2024) found that governance quality mediates the relationship between ESG performance and market valuation through enhanced customer satisfaction and investor confidence.

Nevertheless, the empirical literature presents mixed findings. Some studies, such as Duque-Grisales & Aguilera-Caracuel (2021), revealed a negative relationship between governance and firm value under specific conditions. Others, such as Faure et al. (2024) and An et al. (2024), suggested no significant correlation, indicating that context, measurement, and moderating factors might influence the observed outcomes. This inconsistency highlights the need for further investigation, particularly in emerging markets where governance structures and market dynamics differ from developed economies.

ESG and Market-Based Value

Market-based value, commonly proxied by Tobin's Q, represents how the market perceives a firm's ability to generate future earnings. ESG-adopted firms are expected to have stronger governance frameworks, which can signal lower risk, better stakeholder engagement, and long-term sustainability. These expectations align with signaling theory (Spence, 1973; Ross, 1977), suggesting that firms use observable attributes such as governance performance to convey private information about their quality to external stakeholders.

In this context, ESG-oriented governance can improve a firm's reputation and attract socially responsible investors, ultimately enhancing market valuation. Zhou et al. (2021)

confirmed that firms with higher governance scores tend to maintain healthier capital structures and reduced information asymmetry.

Institutional Ownership as a Moderating Variable

Institutional ownership is widely recognized for its potential to strengthen corporate governance through external monitoring. Institutional investors typically possess the resources, expertise, and incentives to hold management accountable, reduce agency problems (Jensen & Meckling, 1976), and influence strategic decisions. Hartzell & Starks (2003) emphasized that institutional shareholders act as governance enforcers, exerting pressure for transparency and long-term value creation.

However, the role of institutional ownership in moderating the governance-firm value relationship remains underexplored in ESG-specific contexts. While some researchers, like Sakawa (2020) and Velte (2024), affirm its moderating influence, others suggest that its effectiveness varies depending on ownership concentration, investor type, and regulatory environments.

Research Gap

Despite extensive literature on corporate governance and firm value, limited studies explore the moderating role of institutional ownership within ESG-adopted firms in emerging markets like Indonesia. Most prior studies have focused on direct relationships without incorporating ownership structures as potential moderators. Given Indonesia's evolving regulatory landscape and increasing ESG adoption, examining this intersection offers novel insights into how corporate governance effectiveness can be influenced by ownership dynamics.

Theoretical Framework

This study is grounded in agency theory and signaling theory. Agency theory explains the conflict between shareholders and managers due to divergent interests and information asymmetry, mitigated by governance mechanisms. Signaling theory, in turn, emphasizes how governance quality serves as a credible signal to external parties about firm reliability and long-term potential. These theories collectively support the hypotheses that (1) good governance positively influences market value, and (2) institutional ownership strengthens this effect through enhanced monitoring and alignment of interests.

METHODS

This study employs panel data regression analysis to investigate the relationship between corporate governance and market-based firm value, and examines the moderating effect of institutional ownership. The research focuses on companies listed on the Indonesia Stock Exchange during the period 2019-2023. Secondary data were collected from annual reports, sustainability reports, and the Bloomberg database. The Bloomberg Governance Performance Score served as the primary measure of corporate governance quality, while financial data were extracted from audited financial statements. The population comprises all companies listed on the Indonesia Stock Exchange. Through purposive sampling, 161 firms were selected based on the following criteria: (1) listed on the IDX during 2019-2023, (2) having available Bloomberg governance scores data, (3) having complete institutional ownership data, (4) publishing annual reports and sustainability reports, and (5) having complete data for all research variables.

The study incorporates dependent, independent, moderating, and control variables as presented in Table 1. Market-based value (Tobin's Q) serves as the dependent variable, while governance performance (Bloomberg Governance Score) represents the independent variable. Institutional ownership functions as the moderating variable. Control variables include leverage, firm size, growth, and return on equity.

Table 1. Research Variables

Variable	Name of Variable	Measurement Scale	Variable Measurement	Source
TOBINSQ	Market-Base Value	Ratio	Tobin's Q = (Market Value of Equity + Book Value of Debt) / Book Value of Assets	(Seok et al., 2024a)
GOV	Governance Performance	Ratio	Bloomberg Governance Performance Score	(Buchetti et al., 2025)
INST	Institutional Ownership	Ratio	Percentage of shares owned by institutional investors include mutual funds, pension funds, and insurance companies	Nasta et al. (2024)
Control Variables:				
LEV	Leverage	Ratio	Total Debt / Total Assets	(Yu & Xiao, 2022)
SIZE	Corporate Size	Ratio	Natural logarithm of total assets	(Tang et al., 2024a)
GROWTH	Growth	Ratio	(Revenue t - Revenue t-1) / Revenue t-1	(Duan et al., 2023)
ROE	ROE	Ratio	Net Income / Shareholder's Equity	(Faure et al., 2025a)

Source: Data Processed (2025)

The analytical process begins with descriptive statistics to characterize the data. Classical assumption tests are then conducted to ensure the validity of the regression models. Panel model selection involves sequential application of the Chow, Hausman, and Lagrange Multiplier tests to determine the most appropriate estimation approach (random effects). Goodness of fit assessment precedes hypothesis testing, which is performed at the one percent significance level. The study employs two regression models to test the hypotheses:

Base Model: $TOBINSQ_{(i,t)} = \alpha + \beta_1 GOV_{(i,t)} + \beta_2 LEV_{(i,t)} + \beta_3 SIZE_{(i,t)} + \beta_4 GROWTH_{(i,t)} + \beta_5 ROE_{(i,t)} + \epsilon_{(i,t)}$ (1)

Institutional Ownership Moderation: $TOBINSQ_{(i,t)} = \alpha + \beta_1 GOV_{(i,t)} + \beta_2 INST_{(i,t)} + \beta_3 (GOV \times INST)_{(i,t)} + \beta_4 LEV_{(i,t)} + \beta_5 SIZE_{(i,t)} + \beta_6 GROWTH_{(i,t)} + \beta_7 ROE_{(i,t)} + \epsilon_{(i,t)}$ (2)

α indicates the value of the constant, β_1 to β_7 indicates the regression coefficient, and ϵ indicates an error.

RESULTS

Table 2 presents the descriptive statistics of all variables in this study. The mean Tobin's Q value is 0.1420, indicating that on average, the market value of ESG-adopted firms in Indonesia is slightly higher than their book value. Corporate governance performance shows a mean score of 4.3850, with considerable variation among firms (minimum 2.1480, maximum 6.9990). Institutional ownership averages 35.0649% with substantial dispersion (standard deviation of 32.1736), suggesting diverse ownership structures across the sample. The financial control variables reveal that sampled firms maintain an average leverage ratio of 22.1837%, demonstrate modest growth (16.86%), and generate a mean return on equity of 11.2125%.

Table 2. Descriptive Statistics of Research Variables

Variable	Mean	Median	Maximum	Minimum	Std. Dev.
TOBINSQ	0.1420	0.0878	1.0001	-0.2348	0.1866
GOV	4.3850	4.3716	6.9990	2.1480	0.8362
INST	35.0649	20.9608	135.7428	0.0000	32.1736
LEV	22.1837	18.9536	74.3069	-0.2566	18.4488
SIZE	0.0323	0.0553	0.3026	-0.5954	0.1228
GROWTH	0.1686	0.0775	5.8420	-2.6648	0.6141
ROE	11.2125	9.4651	221.3594	-120.2535	25.4848

Source: Research Data, 2025

Before proceeding with hypothesis testing, the study conducted a series of diagnostic tests to determine the most appropriate panel regression model. The Chow test yielded a probability value of 0.0000, initially suggesting a fixed effects model. However, the subsequent Hausman test produced a probability value of 0.6712, indicating that the random effects model was more suitable. Finally, the Lagrange Multiplier test confirmed the random effects specification with a significant probability value of 0.0000. Classical assumption tests for multicollinearity, normality (Jarque-Bera probability of 0.7936), heteroscedasticity, and autocorrelation (Durbin-Watson of 0.8136) revealed no violations of regression assumptions.

The research employed two regression models to examine the study's hypotheses. Model 1 investigated the direct relationship between corporate governance and firm value, while Model 2 incorporated the moderating effect of institutional ownership. The results of Model 1 are presented in Table 3.

Table 3. Panel Regression Results for Model 1 (Direct Effect)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.1313	0.0082	16.0742	0.0000***
GOV	0.0090	0.0014	6.4463	0.0000***
LEV	-0.0010	0.0001	-12.6207	0.0000***
GROWTH	0.0518	0.0010	54.3704	0.0000***
SIZE	-1.3240	0.0101	-131.6176	0.0000***
ROE	0.0031	0.0000	90.1104	0.0000***
R-squared	0.9747			
Adjusted R-squared	0.9745			
F-statistic	4447.1755			0.0000***
Durbin-Watson stat	0.8321			

*** p<.01 Source: Research Data, 2025

Model 1 results demonstrate that corporate governance (GOV) has a significant positive effect on firm value (coefficient = 0.0090, t-statistic = 6.4463, p-value = 0.0000), strongly supporting Hypothesis 1. This finding indicates that each one-unit increase in the governance score is associated with a 0.0090 unit increase in Tobin's Q, holding other factors constant. The model explains 97.47% of the variation in market-based firm value (R-squared = 0.9747), indicating excellent explanatory power.

Among control variables, leverage (LEV) exhibits a significant negative relationship with firm value (coefficient = -0.0010), suggesting that higher debt levels may increase financial risk and reduce market valuations. Growth (GROWTH) and profitability (ROE) both show significant positive relationships with firm value (coefficients of 0.0518 and 0.0031, respectively), consistent with expectations that growing, profitable firms command higher market valuations. Interestingly, firm size (SIZE) displays a strong negative relationship with Tobin's Q (coefficient = -1.3240), possibly indicating that larger firms face greater challenges in maintaining market premiums relative to their asset base.

Table 4 presents the results of Model 2, which incorporates institutional ownership as a moderating variable.

Table 4. Panel Regression Results for Model 2 (Moderation Effect)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.1422	0.0108	13.1129	0.0000***
GOV	0.0068	0.0021	3.1713	0.0016***
LEV	-0.0010	0.0001	-12.7099	0.0000***
GROWTH	0.0517	0.0010	54.2137	0.0000***
SIZE	-1.3219	0.0101	-130.7596	0.0000***
ROE	0.0031	0.0000	90.1584	0.0000***
INST	-0.0003	0.0002	-1.4723	0.1415
GOV*INST	0.0001	0.0000	1.3049	0.1925
R-squared	0.9745			
Adjusted R-squared	0.9742			
F-statistic	3137.0923			0.0000***
Durbin-Watson stat	0.8136			

*** p<.01 Source: Research Data, 2025

DISCUSSION

In Model 2, corporate governance (GOV) maintains its significant positive effect on firm value (coefficient = 0.0068, t-statistic = 3.1713, p-value = 0.0016), though the coefficient is slightly reduced compared to Model 1. However, neither institutional ownership (INST) nor its interaction with governance (GOV*INST) demonstrates statistical significance (p-values of 0.1415 and 0.1925, respectively). These findings do not support Hypothesis 2, suggesting that institutional ownership does not significantly moderate the relationship between corporate governance and market-based firm value in ESG-adopted Indonesian listed companies.

The positive relationship between corporate governance and firm value aligns with signaling theory, as effective governance practices communicate positive signals to market participants regarding management quality, risk management capabilities, and future value creation potential. This finding corroborates previous studies by (Seok et al., 2024a) and (Tang et al., 2024b), which established that robust governance practices enhance market valuations by signaling effective management oversight and strategic direction.

Strong governance frameworks indicate to investors that companies are likely to make decisions aligned with long-term value creation rather than short-term gains or managerial self-interest. This is particularly relevant in ESG-adopted firms, where stakeholders increasingly scrutinize governance practices as indicators of sustainability commitment. The positive relationship supports (Buchetti et al., 2025) assertion that governance quality serves as a credible signal of management capability in complex ESG contexts.

The lack of significant moderation by institutional ownership contradicts our theoretical expectation based on agency theory. Although institutional investors possess the resources and expertise to monitor management effectively, their presence does not appear to enhance the impact of governance on firm value in our sample. This finding diverges from (Velte, 2024) and (Sakawa, 2020). research, which found that institutional ownership strengthened governance effectiveness through sophisticated monitoring mechanisms.

Several factors may explain this unexpected result. First, institutional ownership in the Indonesian market might be characterized by passive investment approaches rather than active engagement with governance matters. Second, the quality and effectiveness of institutional monitoring may vary considerably across different institutional investors, with some taking more active roles than others. Third, the Indonesian regulatory environment might already provide sufficient external monitoring, potentially reducing the marginal impact of institutional oversight.

The control variables offer additional insights into market valuation dynamics. The negative coefficient for leverage supports the view that excessive debt increases financial risk and reduces firm flexibility, adversely affecting market valuations. This aligns with (Yu & Xiao, 2022) findings that financial stability is a key consideration in ESG firm valuations. The positive coefficients for growth and profitability emphasize that fundamentals remain critical drivers of market value, consistent with (Duan et al., 2023) assertion that financial performance enhances capital market access and reduces funding costs.

The strong negative relationship between firm size and Tobin's Q presents an interesting contrast to conventional wisdom. While larger firms typically benefit from economies of scale and market power, they may face challenges in governance implementation due to organizational complexity. This finding suggests that smaller firms might be more agile in implementing effective governance frameworks and responding to ESG expectations, leading to higher relative market valuations.

These results highlight the importance of context in understanding governance-value relationships. In ESG-adopted Indonesian firms, governance quality directly enhances market valuations, but this enhancement operates independently of institutional ownership levels. The findings contribute to the ongoing scholarly conversation about contingency factors in governance effectiveness, suggesting that the market responds positively to governance signals regardless of ownership structure in this particular context.

CONCLUSION

This study investigated the relationship between corporate governance and market-based firm value in ESG-adopted firms listed on the Indonesia Stock Exchange from 2019 to 2023, examining the potential moderating role of institutional ownership. The findings provide strong evidence that corporate governance positively influences market-based firm value, supporting the view that robust governance practices signal effective management and value creation potential to market participants. However, contrary to expectations, institutional ownership does not significantly moderate this relationship, suggesting that market response to governance quality operates independently of institutional monitoring in ESG-adopted Indonesian firms. Additional findings reveal that growth opportunities and profitability enhance market valuations, while leverage and firm size demonstrate negative associations with Tobin's Q.

The study has several limitations that provide avenues for future research. First, the Bloomberg Governance Performance Score may not capture all governance dimensions relevant to the Indonesian context; future studies could develop market-specific governance indices. Second, institutional ownership was treated as homogeneous, whereas different types of institutional investors might exert varying influences on governance effectiveness; further research could disaggregate institutional ownership by investor type. Third, the five-year study period might not capture longer-term governance-value dynamics. Finally, comparative analyses across different emerging markets could identify how country-specific factors influence the governance-value relationship and the moderating role of institutional ownership.

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