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## The Effect ESG and Independent Commissioner on Firm Value

Ernie Hendrawaty<sup>1</sup>, Igo Febrianto<sup>2</sup>

<sup>1,2</sup>Department of Management, Faculty of Economics and Business, University of Lampung, Indonesia

Corresponding email: [ernie.hendrawaty@feb.unila.ac.id](mailto:ernie.hendrawaty@feb.unila.ac.id)

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### Abstract

This study aims to analyze the influence of Environmental, Social, and Governance (ESG) score and the proportion of independent commissioners on firm value among companies listed in the ESG Leaders Index on the Indonesia Stock Exchange. Firm value is proxied by the Cyclically Adjusted Price Earnings Ratio (CAPE Ratio), while ESG score is measured based on Morningstar Sustainalytics ratings and independent commissioners are measured by the proportion of independent commissioners to the total board of commissioners. This study employs a quantitative approach using secondary data obtained from financial statements, sustainability reports, stock price data, index information, and other relevant sources. The sample was determined using a purposive sampling technique and comprised 23 companies that satisfied the established research criteria. The data were analyzed using multiple linear regression techniques with the assistance of Microsoft Excel and JASP software. The results show that ESG score has a positive but statistically insignificant relationship with the CAPE Ratio. Meanwhile, independent commissioners exhibit a negative but statistically insignificant relationship with the CAPE Ratio. These findings indicate that ESG score and independent commissioners are not yet strong determinants of firm value in the observed sample. Future research is suggested to include control, mediating, or moderating variables to provide a more comprehensive explanation of firm value.

## INTRODUCTION

Sustainability issues have become increasingly significant in investment decision-making within capital markets. Investors no longer rely exclusively on traditional financial indicators, but also consider Environmental, Social, and Governance (ESG) aspects as important indicators of corporate sustainability. This development has encouraged the emergence of sustainability-based stock indices, including the ESG Leaders Index on the Indonesia Stock Exchange. The index serves as one of the references for investors in identifying companies that are considered to have better sustainability practices and corporate governance.

Research on ESG has continued to grow in recent years. Previous studies have examined the relationship between ESG and firm value, financial performance, cost of capital, investor perception, ESG rating differences, greenwashing, and the comparison between ESG and non-ESG indices. Yu, Guo, and Luu (2018) found that higher ESG transparency increases firm value, particularly firm value measured using Tobin's Q. Similar findings were reported by Abdi, Li, and Câmara-Turull (2022), Habib and Mourad (2024), and Aydoğmuş, Gülay, and Ergun (2022), who showed that ESG practices may contribute to the improvement of firm value and corporate financial performance. However, the relationship between ESG and firm performance does not always demonstrate consistent results. Several studies found that ESG-related indices or stocks do not always provide significantly better returns than non-ESG indices, while other studies found a negative relationship between ESG and firm performance in certain contexts.

The inconsistency of previous findings indicates that the relationship between ESG and firm value still requires further investigation, especially in the context of the Indonesian capital market. In addition, most previous studies measure firm value using Tobin's Q, Price to Earnings Ratio, Price to Book Value, or other conventional valuation measures. This study uses the Cyclically Adjusted Price Earnings Ratio (CAPE Ratio) as a proxy for firm value. The CAPE Ratio is considered useful because it provides a long-term valuation perspective by comparing current stock prices with average historical earnings that have been adjusted over time.

In addition to ESG, corporate governance is also an important factor in explaining firm value. One governance mechanism that is often discussed is the presence of independent commissioners. Independent commissioners are expected to strengthen the supervisory function of the board and provide objective advice to management in strategic decision-making. Theoretically, a higher proportion of independent commissioners should improve monitoring quality and reduce agency problems. However, in practice, the effect of independent commissioners on firm value may differ depending on their effectiveness, competence, independence, and the market's perception of the company's governance structure.

This study contributes to the literature on ESG and corporate governance by examining the influence of ESG scores and independent commissioners on firm value as measured by the CAPE Ratio. The use of the CAPE Ratio provides a different perspective from previous studies that mostly used conventional valuation measures. Therefore, this study aims to analyze whether ESG score and independent commissioners affect firm value among companies listed in the ESG Leaders Index on the Indonesia Stock Exchange.

## Literature Review and Hypothesis Development

### *Legitimacy Theory*

Legitimacy theory posits that companies seek to ensure that their activities are aligned with the norms, values, and expectations prevailing within society. Companies are not only viewed as economic entities, but also as social institutions that have a social contract with the surrounding community. Brown and Deegan (1998) explain that social and environmental disclosure can be utilized by companies as a means of enhancing legitimacy and maintaining public trust. Through the disclosure of information related to social, environmental, and governance aspects,

companies attempt to demonstrate that their business activities are aligned with public expectations.

In the context of ESG, legitimacy theory explains why companies are encouraged to improve their ESG performance and sustainability disclosure. Companies with better ESG performance may be perceived as more responsible toward the environment, society, and stakeholders. Such perceptions can improve corporate reputation and investor confidence. However, legitimacy may not always be directly reflected in market valuation. Investors' responses to ESG information can be influenced by the quality of disclosure, the credibility of ESG ratings, industry characteristics, and capital market conditions.

### *ESG and Firm Value*

ESG reflects the assessment of a company's practices in environmental, social, and governance dimensions. The environmental dimension relates to the company's efforts to manage environmental impacts, resource efficiency, and environmental risk. The social dimension concerns the company's relationship with employees, customers, communities, and other stakeholders. The governance dimension relates to board structure, transparency, accountability, and monitoring mechanisms.

Several previous studies have demonstrated that ESG practices can enhance firm value. Yu, Guo, and Luu (2018) found that ESG transparency has a positive relationship with firm value. Chang and Lee (2022) also found that ESG activities positively affect firm value in South Korea. Aydoğmuş, Gülay, and Ergun (2022) showed that ESG performance is related to firm value and profitability. These findings indicate that ESG practices may provide a positive signal to investors regarding the company's long-term prospects and sustainability performance.

However, the relationship between ESG and firm value remains inconclusive, as empirical findings across previous studies have produced mixed results. Differences in ESG rating standards across rating agencies can lead to different investor interpretations. Billio et al. (2021) highlighted differences in characteristics, attributes, and standards used to define ESG components. Horn and Oehler (2024) also found that different ESG rating providers may produce different portfolio outcomes. Therefore, the effect of ESG on firm value may depend on market context and the quality of ESG information used by investors.

Based on the above explanation, the first hypothesis is formulated as follows:

H1: ESG score has a positive effect on firm value.

### *Independent Commissioners and Firm Value*

Independent commissioners are members of the board of commissioners who do not have financial, managerial, ownership, or familial relationships with controlling shareholders, directors, or other members of the board of commissioners that could compromise their independence. The presence of independent commissioners is expected to strengthen the supervisory function and improve the quality of corporate governance.

Previous studies have shown that board characteristics may affect corporate disclosure quality and firm performance. Donnelly and Mulcahy (2008), Tahir, Masri, and Rahman (2020), and Vitolla, Raimo, and Rubino (2020) showed that board independence, size, activity, and diversity may be associated with disclosure quality and corporate policy. Independent commissioners can help mitigate conflicts of interest between management and shareholders by providing more objective and impartial oversight.

Nevertheless, the effect of independent commissioners on firm value is not always positive. García-Sánchez and Martínez-Ferrero (2017) found that independent directors may show resistance to CSR disclosure practices under certain conditions. Moreover, a higher proportion of independent commissioners does not necessarily improve firm value if their role is

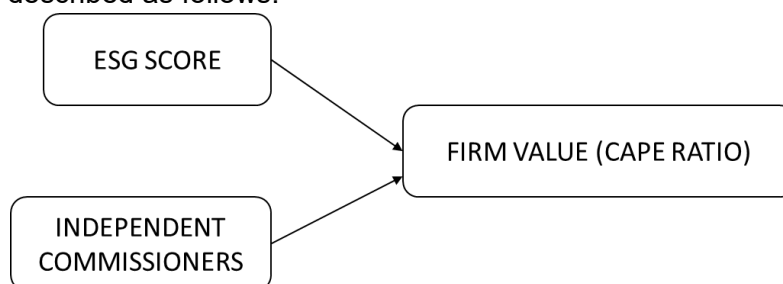
merely formal and not supported by effective supervision. Therefore, the effect of independent commissioners on firm value needs to be empirically tested.

Based on the above explanation, the second hypothesis is formulated as follows:

H2: Independent commissioners have a positive effect on firm value.

### **Conceptual Framework**

This study examines the effect of ESG score and independent commissioners on firm value. Firm value is proxied by the CAPE Ratio. ESG score represents the quality of corporate sustainability practices, while independent commissioners represent the supervisory structure within corporate governance. Conceptually, better ESG performance and a higher proportion of independent commissioners are expected to improve firm value. The conceptual framework of this study can be described as follows:



**Figure 1. Research Framework**

## **RESEARCH METHODOLOGY**

This study employs a quantitative approach using secondary data. The population comprises all companies included in the ESG Leaders Index on the Indonesia Stock Exchange during the observation period. The sample was determined using a purposive sampling technique, which involves selecting samples based on criteria relevant to the research objectives.

The sample criteria include companies that were consistently included in the ESG Leaders Index during the observation period and had the required data, including financial statements, sustainability reports, stock price data, ESG scores, and information on the composition of the board of commissioners. Based on these criteria, 23 companies were selected as the research sample. The data were obtained from the Indonesia Stock Exchange website, company financial statements, company sustainability reports, and other relevant sources.

The dependent variable in this study is firm value, proxied by the CAPE Ratio. The CAPE Ratio is a valuation ratio that compares current stock prices with the company's long-term average earnings. This ratio is used to evaluate whether a company's stock price is undervalued, fairly valued, or overvalued. The use of the CAPE Ratio is expected to provide a more stable long-term perspective of firm value.

The first independent variable is ESG score. ESG score in this study is measured based on Morningstar Sustainalytics ratings. The ESG score reflects the company's level of ESG risk or sustainability performance in environmental, social, and governance dimensions. The second independent variable is independent commissioners, which are measured by the proportion of independent commissioners relative to the total number of members on the board of commissioners.

The data analysis technique employed in this study is multiple linear regression analysis. Before conducting regression analysis, descriptive statistics were used to identify the minimum, maximum, mean, median, and standard deviation of each variable. Data processing was carried out using Microsoft Excel and JASP. The regression model is formulated as follows:

$$FV = \beta_0 + \beta_1 ESG + \beta_2 IC + \varepsilon$$

Where:

- FV* = firm value proxied by the CAPE Ratio  
*ESG* = ESG score  
*IC* = proportion of independent commissioners  
 $\beta_0$  = constant  
 $\beta_1, \beta_2$  = regression coefficients  
 $\varepsilon$  = error term

**Table 1.**  
**Operational Definition of Variables**

Variable	Symbol	Measurement	Scale	Source
Firm Value	FV	Stock price divided by long-term average earnings (Cyclically Adjusted Price Earnings Ratio)	Ratio	IDX, financial statements
ESG Score	ESG	ESG risk score based on Morningstar Sustainalytics	Ratio	Sustainalytics
Independent Commissioners	IC	Number of independent commissioners / total commissioners	Ratio	Annual report

Source: Author, 2024

## RESULTS AND DISCUSSION

### Descriptive Statistics

The descriptive statistics indicate that all 23 observations are valid and that no missing data were identified. The descriptive statistics for each variable are presented in Table 2.

**Table 2.**  
**Descriptive Statistics**

Variable	N	Median	Mean	Std. Deviation	Minimum	Maximum
ESG	23	20.310	20.772	4.852	10.960	28.650
Independent Commissioners	23	0.500	0.487	0.125	0.330	0.830
CAPE Ratio	23	11.610	14.664	12.355	2.880	53.910

Source: Author, 2024

The mean ESG score of 20.772 indicates that the sample companies generally fall into the medium ESG risk category. The minimum ESG score of 10.960 indicates that some companies have relatively low ESG risk, while the maximum value of 28.650 indicates that some companies have higher ESG risk compared to others in the sample. The standard deviation of 4.852 indicates variation in ESG scores across companies.

The mean value of independent commissioners is 0.487, indicating that the proportion of independent commissioners in the sample companies is, on average, 48.7% of the total board of commissioners. The minimum value of 0.330 indicates that some companies have independent commissioners representing approximately 33% of the board, while the maximum value of 0.830 indicates that some companies have a very high proportion of independent commissioners.

The mean CAPE Ratio of 14.664 indicates that, on average, the valuation of the sample companies is relatively reasonable. The minimum value of 2.880 indicates that some companies have relatively low valuations, while the maximum value of 53.910 indicates that some companies have very high valuations. The standard deviation of 12.355 indicates that the variation in firm value among the sample companies is relatively large.

### Model Summary

The model summary shows an R value of 0.326. This indicates that the relationship between ESG score, independent commissioners, and the CAPE Ratio is relatively weak. The R<sup>2</sup> value of 0.106 indicates that ESG score and independent commissioners explain only 10.6% of the variation in the CAPE Ratio. The remaining 89.4% is explained by other variables outside the model. The adjusted R<sup>2</sup> value of 0.017 indicates that the model's explanatory power remains very low after adjustment for the number of independent variables.

**Table 3.**  
**Model Summary**

Model	R	R <sup>2</sup>	Adjusted R <sup>2</sup>	RMSE
M0	0.000	0.000	0.000	12.355
M1	0.326	0.106	0.017	12.251

Source: Author, 2024

The ANOVA results show an F-statistic of 1.187 with a significance value of 0.326. Since the significance value exceeds 0.05, the regression model is not statistically significant. This means that ESG score and independent commissioners jointly do not significantly explain the CAPE Ratio in the observed sample.

**Table 4.**  
**ANOVA Results**

Model	Sum of Squares	df	Mean Square	F	p
Regression	356.387	2	178.193	1.187	0.326
Residuals	3001.599	20	150.080		
Total	3357.985	22			

Source: Author, 2024

### Regression Results

The regression results show that the coefficient of independent commissioners is negative at -14.274, with a t-value of -0.643 and a significance value of 0.527. This indicates that independent commissioners have a negative but statistically insignificant relationship with the CAPE Ratio. Therefore, H2 is not supported.

The coefficient of ESG score is positive at 0.628, with a t-value of 1.096 and a significance value of 0.286. This indicates that ESG score has a positive but statistically insignificant relationship with the CAPE Ratio. Therefore, H1 is not statistically supported, although the direction of the relationship is consistent with the initial expectation.

**Table 5.**  
**Regression Coefficients**

Variable	Coefficient	Std. Error	Standardized	t	p
Constant	8.567	18.770		0.456	0.653
ESG	0.628	0.573	0.247	1.096	0.286
Independent Commissioners	-14.274	22.188	-0.145	-0.643	0.527

Source: Author, 2024

Based on the regression results, the regression equation is as follows:

$$FV = 8.567 + 0.628ESG - 14.274IC + \varepsilon$$

The equation shows that if independent commissioners and ESG score are assumed to be zero, the CAPE Ratio is 8.567. The coefficient of independent commissioners of -14.274 indicates that an increase in the proportion of independent commissioners tends to be followed by a decrease in the CAPE Ratio, assuming other variables remain constant. However, because the significance value is greater than 0.05, this relationship cannot be concluded as statistically significant. The coefficient of ESG score of 0.628 indicates that an increase in ESG score tends to be followed by an increase in the CAPE Ratio, but this relationship is also not statistically significant.

### **Discussion of the Effect of ESG Score on Firm Value**

The results show that ESG score has a positive but statistically insignificant relationship with firm value proxied by the CAPE Ratio. The positive direction indicates that companies with higher ESG scores tend to have higher CAPE Ratios. Theoretically, this finding is consistent with legitimacy theory, which suggests that companies that pay attention to environmental, social, and governance aspects may obtain positive perceptions from investors and stakeholders.

However, the insignificant result indicates that ESG score is not yet a dominant factor in determining firm value in the sample of this study. Several explanations may support this finding. First, investors in the Indonesian capital market may continue to place greater emphasis on traditional financial indicators, such as profitability, earnings growth, stock liquidity, leverage, industry risk, and macroeconomic conditions. Second, ESG information may still be perceived as supplementary information rather than a primary determinant of investment decisions. Third, the limited sample size may reduce the statistical power of the model, thereby making the relationship between variables less observable.

This finding differs from previous studies that found a positive and significant effect of ESG on firm value, such as Yu, Guo, and Luu (2018), Chang and Lee (2022), and Aydoğmuş, Gülay, and Ergun (2022). However, the result is consistent with the view that the effect of ESG on firm value is not always uniform across markets and sectors. Caporale et al. (2022), La Torre et al. (2020), and Górká and Kuziak (2022) showed that ESG-based indices or companies do not always perform significantly differently from non-ESG alternatives. Therefore, the effect of ESG on firm value may depend on market maturity, investor awareness, disclosure quality, and the credibility of ESG information.

### **Discussion of the Effect of Independent Commissioners on Firm Value**

The results show that independent commissioners have a negative but statistically insignificant relationship with firm value proxied by the CAPE Ratio. This finding indicates that a higher proportion of independent commissioners tends to be associated with a lower CAPE Ratio, although the relationship is not statistically strong enough to be considered significant.

Theoretically, independent commissioners are expected to enhance the quality of monitoring and strengthen corporate governance practices. However, the results of this study indicate that the presence of independent commissioners is not necessarily perceived positively by the market, as reflected in the absence of a higher CAPE Ratio. This may occur if investors perceive the composition of independent commissioners as a matter of regulatory compliance rather than evidence of effective supervision. In other words, a higher number of independent commissioners does not necessarily reflect better monitoring quality.

The negative direction may also be explained by the possibility that companies with a higher proportion of independent commissioners tend to be more cautious in strategic decision-making. Stronger monitoring may reduce excessive risk-taking, but it may also make companies less aggressive in pursuing short-term growth opportunities. Since the CAPE Ratio reflects market

expectations regarding earnings and long-term valuation, this conservative tendency may lead the market to assign a lower valuation to such companies.

This finding does not support the initial hypothesis that independent commissioners positively affect firm value. However, it is consistent with the view that the effectiveness of independent commissioners is not determined solely by their proportion, but also by their competence, experience, substantive independence, meeting frequency, monitoring quality, and involvement in strategic decision-making. Therefore, future research should consider broader governance dimensions rather than relying only on the proportion of independent commissioners.

## **CONCLUSION AND RECOMMENDATION**

### **Conclusion**

This study aims to examine the effect of ESG score and independent commissioners on firm value among companies listed in the ESG Leaders Index on the Indonesia Stock Exchange. Firm value is proxied by the CAPE Ratio. Based on the regression analysis, ESG score has a positive but statistically insignificant relationship with the CAPE Ratio. This indicates that an increase in ESG score tends to be followed by an increase in firm value, but the effect is not strong enough to explain firm value significantly.

Independent commissioners have a negative but statistically insignificant relationship with the CAPE Ratio. This result indicates that the proportion of independent commissioners has not been proven to increase firm value in the sample of this study. Therefore, both hypotheses are not statistically supported. Simultaneously, ESG score and independent commissioners are also unable to significantly explain the CAPE Ratio. The low  $R^2$  value indicates that most of the variation in the CAPE Ratio is explained by other factors outside the research model.

Theoretically, this study contributes to the literature by using the CAPE Ratio as a proxy for firm value in ESG and corporate governance research. The use of the CAPE Ratio provides a long-term perspective on firm valuation. Practically, the findings suggest that companies should continue to improve ESG practices and corporate governance quality, even though their effects on market valuation are not yet statistically significant. Good ESG and governance practices remain important for building reputation, reducing risk, and strengthening long-term investor confidence.

This study has several limitations. First, it only uses two independent variables, namely ESG score and independent commissioners, so the model's ability to explain firm value remains limited. Second, the sample consists of only 23 companies, which limits the generalizability of the findings. Third, the study focuses only on the Indonesian capital market, so the results may not be applicable to countries with different market characteristics and ESG regulations.

### **Recommendation**

Based on these limitations, future research is suggested to include control variables such as firm size, profitability, leverage, liquidity, firm age, industry sector, sales growth, and systematic risk. Future studies may also include mediating or moderating variables, such as sustainability disclosure quality, institutional ownership, foreign ownership, auditor reputation, or macroeconomic conditions. In addition, future research may expand the sample by comparing ASEAN countries or other regions to obtain a more comprehensive understanding of the effect of ESG and corporate governance on firm value.

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