

# THE MEDIATING ROLE OF FINANCIAL PERFORMANCE ON SUSTAINABILITY REPORTING AND FIRM VALUE: A LITERATURE REVIEW

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## Abstract:

This study examines the impact of Sustainability Reporting on firm value in the industrial sector companies listed on the Indonesia Stock Exchange for the 2022-2024 period, using financial performance as a mediating variable. This article employs a literature review approach to synthesize various empirical findings and theoretical frameworks, specifically Signaling Theory and Stakeholder Theory. The findings indicate that sustainability reporting serves as a quality signal to reduce information asymmetry for investors. Furthermore, these practices contribute to operational efficiency, which enhances the company's financial performance. Financial performance acts as a significant mediator in transmitting the impact of sustainability reporting on the increase in firm value. Company management should optimize sustainability reporting strategies as a strategic instrument to enhance firm valuation in the capital market (Ghozali, 2021).

**Keywords: Sustainability Reporting; Firm Value; Financial Performance; Industrial Sector.**

## Abstrak:

Penelitian ini menganalisis pengaruh Sustainability Reporting terhadap nilai perusahaan pada sektor industri di Bursa Efek Indonesia periode 2022-2024 dengan kinerja keuangan sebagai variabel mediasi. Artikel ini menggunakan metode studi literatur untuk mensintesis berbagai temuan empiris serta kerangka teoritis, khususnya Signaling Theory dan Stakeholder Theory. Hasil sintesis menunjukkan bahwa pengungkapan keberlanjutan berfungsi sebagai sinyal kualitas untuk mengurangi asimetri informasi bagi investor. Selain itu, praktik tersebut berkontribusi pada efisiensi operasional yang meningkatkan kinerja keuangan perusahaan. Kinerja keuangan berperan secara signifikan sebagai variabel mediasi dalam mentransmisikan dampak pengungkapan keberlanjutan terhadap peningkatan nilai perusahaan. Pihak manajemen perusahaan sebaiknya mengoptimalkan strategi pelaporan keberlanjutan sebagai instrumen strategis untuk meningkatkan valuasi perusahaan di pasar modal (Ghozali, 2021).

**Kata Kunci: Pengungkapan Keberlanjutan; Nilai Perusahaan; Kinerja Keuangan; Sektor Industri.**

## 1. Introduction

Firm value essentially represents how the market evaluates a management's success in utilizing resources to maximize shareholder wealth. Nowadays, this indicator relies on more than just short-term financial gains; it also captures how investors respond to the company's future growth prospects (Linh et al., 2022). Therefore, industrial companies listed on the Indonesia Stock Exchange (IDX) must maintain their credibility and transparency to ensure their market valuation remains optimal amid fierce economic competition.

In creating this value, financial performance acts as the main bridge. Profitability and operational efficiency, as reflected in financial ratios, provide investors with concrete evidence of the company's fundamental health. Drawing from Signaling Theory, stable financial performance sends a positive signal to the capital market, indicating that the company has the operational resilience to face various economic risks (Brigham & Houston, 2019). Without strong financial performance, investors will likely question the company's ability to sustain its profitability growth.

At the same time, Sustainability Reporting (SR) has emerged as a new strategic tool to strengthen corporate legitimacy and value. When industrial companies disclose their environmental, social, and governance (ESG) responsibilities, they indirectly reduce the information asymmetry between management and stakeholders. This reporting practice goes beyond mere regulatory compliance; it signals that the company has achieved better operational efficiency through sustainable resource management. Often, a company's financial performance improves as a direct result of the efficiencies gained from environmental management practices detailed in these sustainability reports.

Based on this framework, this article analyzes the relationship between Sustainability Reporting and firm value, positioning financial performance as a mediating variable. This study synthesizes various empirical findings to explain how sustainability reporting transmits positive signals that trigger improved financial performance, which ultimately drives firm value growth. This analysis is particularly relevant given the challenges faced by the industrial sector during the 2022-2024 period, which demanded high adaptability to new sustainability-based reporting standards.

## 2. Literatur Review

Signaling Theory serves as the primary foundation for understanding how information transparency shapes market perception. Corporate management utilizes strategic publications to send positive signals to the capital market, ultimately reducing the information asymmetry between internal and external parties (Hanifah et al., 2022). Through this framework, the level of operational openness and financial achievements function as fundamental signals that illustrate the entity's future growth prospects. Consequently, investors heavily rely on these fundamental signals to evaluate the overall quality and resilience of the business.

As a tangible manifestation of these fundamental signals, sustainability reporting disclosures reflect the quality of an entity's risk management. Industrial companies that routinely report their environmental, social, and governance responsibilities demonstrate a strong commitment to sustainable resource management (Linh et al., 2022). This publication informs the public that the company does not merely fulfill regulatory obligations but actively mitigates long-term ecological risks. The capital market then interprets this structured risk management as concrete evidence that the entity possesses excellent operational efficiency (Sari & Andreas, 2019).

This operational efficiency subsequently has a direct impact on measurable financial performance. Applying sustainability principles in daily business activities helps industrial companies reduce waste and optimize profit margins (Aydoğmuş et al., 2022). Although environmental preservation initiatives can build positive initial sentiment, rational investors still demand tangible proof in the form of profitability stability before they decide to reward the company with higher stock prices (Zhou et al., 2022).

## 3. Research Method

This research adopts a literature review method as its primary design without involving statistical testing or field data collection. The researchers focus the study on gathering, examining, and synthesizing various academic literature relevant to the research topic. This approach is chosen so that the researchers can comprehensively elaborate on how sustainability reporting practices interact with financial performance to influence firm value.

Firm value and its forming variables are subsequently dissected through a structured literature search. The literature search process is conducted by utilizing online academic databases, such as Google Scholar and accredited journal portals. The researchers employ a series of specific keywords encompassing firm value, financial performance, sustainability reporting, and the industrial sector to identify relational patterns among the variables based on theoretical foundations and prior empirical findings (Hanifah et al., 2022).

These prior empirical findings are strictly limited to scientific journal articles and sustainability reports published within the last five years. This publication timeframe restriction aims to ensure information novelty, particularly in capturing the dynamics of the industrial sector throughout the 2022–2024 period. Once the literature is collected, the researchers compare the results of these studies to weave the partial findings into a logical flow of thought regarding the mediating mechanism of financial performance.

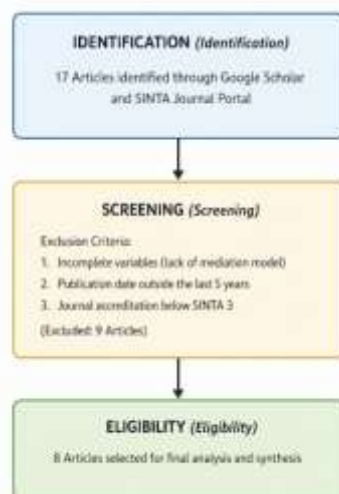
## 4. Results and Discussion

### 4.1 Literature Selection Procedure

This research adopts a systematic literature review approach to identify, evaluate, and synthesize relevant literature concerning the interaction between sustainability reporting, financial performance, and

firm value. The initial identification phase was conducted through academic databases such as Google Scholar and the SINTA journal portal, yielding 17 potential articles. Subsequently, the researcher applied rigorous inclusion and exclusion criteria to ensure the quality of the references. These criteria include: (1) completeness of the research model, which must encompass the mediation relationship between the independent, mediating, and dependent variables; (2) publication timeframe, limited to the last five years (2022–2026); and (3) journal quality, restricted to SINTA 1 to SINTA 3 accredited journals. Following this systematic screening process, 9 articles were excluded for failing to meet the established criteria, leaving 8 primary articles that form the core basis for this study’s analysis.

Figure 1. Literature Selection Flowchart



The literature review results indicate a consistent and mutually reinforcing pattern between sustainability reporting practices and firm value within the industrial sector. Most empirical findings over the past five years convincingly confirm that transparent ESG (Environmental, Social, and Governance) disclosure is not merely an administrative obligation but a strategic instrument to drive operational efficiency. This phenomenon aligns perfectly with Signaling Theory, where companies that voluntarily and openly publish their environmental responsibilities earn significantly higher appreciation from the capital market (Linh et al., 2022; Aydoğmuş et al., 2022). A summary of the key literature synthesis that serves as the foundation for this analysis is presented systematically in Table 1.

Table 1. Summary of Previous Studies

No	Author (Year)	Research Focus	Main Findings
1	Suhartini et al. (2024)	SR, Governance & Value	Financial performance does not fully mediate the SR-Value relationship.
2	Zhou et al. (2022)	ESG & Market Value	Financial performance acts as a significant mediating variable.
3	Asni & Agustina (2022)	Green Innovation & Value	Financial performance bridges the effect of innovation on firm value.
4	Aydoğmuş et al. (2022)	ESG, Profitability & Value	ESG positively impacts both profitability and firm value.
5	Linh et al. (2022)	SR & Firm Value	SR shows a significant positive relationship with firm valuation.
6	Sari & Andreas (2019)	SR & Financial Performance	SR disclosure promotes long-term operational cost efficiency.
7	Yuliyanti et al. (2022)	Financial Performance & Value	Financial performance is a key signal for investor perception of value.
8	Atan et al. (2018)	SR Impact & Firm Value	Environmental disclosure affects value through financial gains.

As summarized in Table 1, the operational efficiency resulting from sustainability practices serves as the primary catalyst for enhancing a company's financial performance. Based on the synthesis of these various studies, companies that integrate sustainability aspects into their daily management are proven capable of reducing unproductive expenses while optimizing resource utilization. This condition clarifies that sustainability reporting serves as a "tangible efficiency signal" for investors, an argument supported by the findings of Sari & Andreas (2019) and Zhou et al. (2022), who suggest that investments in eco-friendly technology ultimately benefit the company in the long run.

Although sustainability reports provide positive signals, financial performance retains a crucial role as a mediating variable that connects these disclosures to firm value. Rational investors, as highlighted by Yuliyanti et al. (2022), tend to be more responsive to fundamental results such as profitability stability and earnings growth as concrete evidence of the qualitative signals provided by the company. Ultimately, the integration of both sustainability signals and solid financial performance triggers investor confidence, thereby creating higher firm value in a sustainable manner, as evidenced by the convergence of empirical findings in recent years (Linh et al., 2022; Asni & Agustina, 2022).

## 4.2 Discussion

### 4.2.1 Sustainability Reporting as a Tangible Efficiency Signal

The empirical evidence synthesized in this review consistently highlights that sustainability reporting functions as far more than just a regulatory compliance requirement; it operates as a sophisticated strategic communication tool. Grounded in Signaling Theory, the disclosure of Environmental, Social, and Governance (ESG) information acts as a conduit to reduce the persistent information asymmetry that exists between corporate management and external stakeholders. By proactively disclosing non-financial information, companies essentially signal their high-quality management standards and long-term risk mitigation capabilities to the capital market.

As Sari & Andreas (2019) and Zhou et al. (2022) have argued, the positive market reaction to sustainability disclosures is intrinsically linked to the underlying operational efficiency. Investors no longer view sustainability reports as mere marketing documents; instead, they scrutinize the data to evaluate how effectively a company manages its resources. When a firm successfully converts environmental initiatives into cost savings through energy reduction, waste management, or green supply chain optimization, the market recognizes these actions as indicators of superior operational excellence. Thus, the reporting of these initiatives serves as a tangible efficiency signal, providing the market with assurance that the company is well-prepared to navigate the challenges of a green economy while maintaining a competitive advantage in the industrial sector.

### 4.2.2 The Mediating Role of Financial Performance in Enhancing Firm Value

A central finding of this review is that the relationship between sustainability disclosure and firm value is essentially a sequential process mediated by financial performance. While some studies suggest a direct impact, our synthesis of the selected eight articles highlights that sustainability initiatives must first be processed through the company's financial system to generate value. This mediation effect is grounded in the reality that sustainability is an investment; for this investment to translate into firm value, it must manifest in tangible financial metrics such as improved profit margins, return on assets, or operational cost reduction.

Rational investors, as emphasized by Yuliyanti et al. (2022), prioritize fundamental performance as the ultimate verification of a company's health. The mediating mechanism operates where sustainability-driven operational improvements lead to enhanced financial robustness, and it is this robust financial performance that ultimately justifies a higher market valuation. This sequential logic is corroborated by Asni & Agustina (2022) and Linh et al. (2022), who suggest that firm value is not a static result of reporting, but a dynamic outcome of how well a company converts its sustainability-driven operational efficiencies into profit.

Furthermore, while Suhartini et al. (2024) introduced a more nuanced perspective suggesting that this mediation is not universal, the prevailing consensus in the empirical literature indicates that the synergy between non-financial reporting and financial excellence is the most reliable driver of firm value. Therefore, it is no longer sufficient for companies to disclose sustainability efforts in isolation. To maximize shareholder wealth, management must ensure that their sustainability strategy has a direct, observable, and positive impact on the company's bottom line. The integration of qualitative ESG signals

and quantitative financial results is, therefore, the fundamental requisite for building sustainable corporate value in the modern industrial landscape.

## 5. Conclusion

This study provides a comprehensive synthesis of the relationship between sustainability reporting, financial performance, and firm value. Based on the analysis of 8 selected primary articles, several key conclusions can be drawn. First, sustainability reporting acts as a strategic "efficiency signal" rather than a mere administrative burden. Companies that transparently disclose their ESG commitments effectively reduce information asymmetry, thereby gaining greater trust and appreciation from the capital market. The evidence confirms that sustainability-driven operational efficiency is a core determinant of a company's long-term competitive advantage.

Second, this research underscores the critical mediating role of financial performance. The synthesis of empirical findings confirms that the impact of sustainability reporting on firm value is not always direct; instead, it is largely channeled through improved financial health. Sustainable practices such as eco-friendly innovation and resource optimization significantly enhance operational efficiency, which in turn boosts profitability. For rational investors, this strong financial performance serves as the final, concrete validation required to convert qualitative sustainability signals into higher firm value. Therefore, the integration of non-financial sustainability data and robust financial metrics is essential for companies aiming to maximize market valuation in a sustainable manner.

Finally, while this study confirms the prevailing positive relationship between these variables, it also acknowledges that the mediation effect may vary depending on organizational context, as highlighted by the contrasting findings in some literature. Consequently, future research is encouraged to expand the scope of analysis across different industrial sectors or utilize primary empirical data to further validate these mediation mechanisms. For practitioners, this study serves as a clear directive that corporate sustainability strategies must be aligned with sound financial management to ensure that environmental and social initiatives translate into tangible value for both shareholders and stakeholders.

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