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EXPLORING THE RELATIONSHIP BETWEEN ESG REPORTING FACTORS AND PERFORMANCE

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ABSTRACT

The environmental, social, and governance (ESG) factors are receiving more and more attention in the research. This study aims to examine the connection between ESG variables and organizational performance. Businesses that emphasize environmental sustainability, social responsibility, and good governance typically achieve better financial results, have highly satisfied employees and can draw in and hold on to clients and investors concerned about moral and responsible business practices. This study employs a quantitative research methodology to explore the relationship between ESG reporting factors and performance. The data for this research is extracted from the annual reports of 160 companies operating in different European countries. The results suggest that organizations that prioritize environmental sustainability, social responsibility, and effective governance practices are more likely to experience better financial performance. These findings have implications for both practitioners and policymakers, highlighting the importance of incorporating ESG considerations into business strategies to enhance financial performance.

KEYWORDS: ESG factors, environmental factors, social factors, governance factors, corporate governance, organizational performance.

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INTRODUCTION

ESG reporting has become increasingly prominent as businesses acknowledge the significance of addressing sustainability issues and showcasing their commitment to responsible practices. ESG reporting encompasses the disclosure of non-financial information pertaining to an organization's environmental impact, social practices, and governance structure. It covers factors such as carbon emissions, employee diversity, board composition, and ethical standards. The purpose of ESG

reporting is to promote transparency among stakeholders, including investors, employees, customers, and communities, regarding an organization's environmental and social performance.

In recent years, companies have faced greater scrutiny regarding their management practices and their impact on people and the environment (Sandberg, Alnoor, and Tiberius, 2022; Girneata et al., 2015). Investors, consumers, and other stakeholders now seek businesses that align with their values and interests, as the importance of ESG issues becomes more widely recognized (Gillan et al., 2010). This recognition is crucial because studies have indicated that businesses that prioritize ESG concerns often achieve superior financial outcomes, enjoy higher employee satisfaction, and engage more effectively with clients.

The objective of this research is to identify the ESG factors that may influence business performance. By answering this question, valuable insights can be gained on how companies can approach ESG issues to enhance their overall performance. The study achieves this by conducting a comprehensive review of the existing literature on ESG components and their impact on company success. Additionally, a practical analysis of 160 European companies is conducted to provide real-world insights. The research incorporates perspectives from various academic disciplines and geographical areas to ensure a comprehensive understanding of the topic at hand. Moreover, the study examines specific ESG components known to affect company success, thereby contributing to the existing body of knowledge in this area.

LITERATURE REVIEW

The recognition of the significance of ESG aspects in corporate governance has grown recently as investors, customers, and other stakeholders have increasingly focused on these issues (Dorfleitner, Halbritter, and Nguyen, 2015). Businesses are now tasked with addressing these challenges to improve their performance and align with the values and objectives of stakeholders.

Three key categories of ESG factors are governance, social, and environmental. Each area encompasses specific ESG factors that are defined, accompanied by a brief explanation of their impact on business performance. To illustrate the practical application of these factors, case studies and examples are presented for each ESG aspect considered. Furthermore, an evaluation of the relationship between each ESG element and performance is conducted. The findings from the environmental, social and governance domains are then aggregated and integrated into the final section of the review.

This approach allows for a comprehensive analysis of the diverse ESG aspects, their implications for business performance, and the interplay between them. By examining real-world cases and combining insights from various ESG areas, this research contributes to a comprehensive understanding of the subject matter.

2.1. Environmental Factors

An organization's environmental impact is assessed using a range of parameters, such as carbon emissions, energy consumption, waste management, resource conservation, and more (Gillan et al., 2010). Increasing concerns about climate change and environmental sustainability are influencing

these aspects, placing greater pressure on businesses to adopt sustainable practices and reduce their environmental footprint (Abdissa et al., 2022). Environmental considerations are of utmost importance for organizations to address, as they can significantly impact corporate success (Cuc et al., 2025). According to Almeyda and Darmansya (2019), companies that prioritize environmental sustainability are more likely to experience improved financial outcomes and can attract and retain clients who value environmental responsibility.

Environmental factors exert a significant influence on an organization's performance. While the relationship between environmental practices, ESG (environmental, social, and governance) measures, and financial performance has received considerable research attention, the connection between ESG practices and corporate environmental performance has been less explored. Some studies suggest a negative correlation between environmental disclosure and environmental performance, indicating that well-designed environmental regulations can stimulate innovation, reduce compliance costs, enhance business competitiveness, and ensure financial viability. Drawing on legitimacy and stakeholder theories proposed by Deep house and such man (2008), organizations engage stakeholders and maintain legitimacy by incorporating ESG principles into their operations. Sharing environmental data can also help investors and stakeholders better comprehend an organization's responsibilities. To enhance both environmental and economic performance, this paper offers guidance to organizations on establishing an environmental management framework and integrating ESG principles into decision-making processes.

The relationship between environmental reporting factors and firm performance has been extensively studied and debated. Trifu et al. (2014) highlight the significant impact of natural factors, such as environmental conditions, climate change, and resource availability, on organizational activities. Understanding the connection between environmental reporting factors and firm performance is crucial for organizations striving to integrate sustainability into their business practices and for investors interested in evaluating the environmental performance of companies. The existing body of literature provides valuable insights into various aspects of this relationship.

Academically, several studies have emphasized the positive influence of robust environmental reporting on firm performance. For instance, Ioannou and Serafeim (2017) discovered a positive correlation between environmental disclosure and financial performance, suggesting that organizations disclosing more environmental information tend to exhibit better financial outcomes. Similarly, Arora and Dharwadkar (2011) found that environmental reporting positively affects organizational reputation, leading to improved financial performance and stakeholder relationships. Whetman (2018) demonstrated a positive association between environmental reporting transparency and firm profitability.

Furthermore, environmental reporting is linked to enhanced operational efficiency. Cubilla-Montilla et al. (2020) highlighted a positive relationship between environmental reporting and eco-efficiency, indicating that organizations reporting their environmental performance are more likely to implement eco-efficient practices and achieve cost savings in their operations.

The relationship between environmental reporting and firm performance is also influenced by various contextual factors. Industry characteristics, for example, play a significant role in shaping this relationship. Li and Liu (2018) discovered that the positive impact of environmental reporting on firm value was more pronounced in environmentally sensitive industries, underscoring the importance of considering industry-specific factors.

Moreover, the regulatory environment and stakeholder pressures impact the relationship between environmental reporting and firm performance. Bednárová et al. (2019) demonstrated that firms operating in regions with stricter environmental regulations tend to exhibit a stronger positive relationship between environmental reporting and financial performance.

Contrasting viewpoints exist in the academic literature regarding the relationship between environmental reporting and financial performance. Some studies have yielded inconclusive or mixed findings. Russo and Harrison (2005), in their meta-analysis of prior studies, found a weak or nonexistent correlation between environmental reporting and financial performance. Such results suggest that the relationship may be context-dependent and influenced by various factors.

However, measuring the precise impact of environmental reporting on firm performance presents methodological challenges. The complex nature of environmental issues, the existence of diverse reporting frameworks, and the limited standardization of measurements make it difficult to establish a direct causal relationship. Additionally, understanding the specific mechanisms through which environmental reporting factors influence performance necessitates careful analysis.

Contextual factors also play a significant role in shaping the relationship between environmental reporting and firm performance. Industry characteristics, firm size, stakeholder pressures, and regulatory environments can moderate this relationship. For instance, Delmas and Pekovic (2018) found that the impact of environmental reporting on firm performance is contingent upon the regulatory context and the level of stakeholder pressure within the industry.

2.2. Social Factors

Social considerations encompass a company's employment practices, adherence to human rights, and engagement with the community. The significance of these issues has grown as concerns regarding ethical and moral business behavior have heightened. Research acknowledges the vital role played by human resources in driving organizational success (Potcovaru & Girneata, 2015). Alsayegh, Abdul Rahman, and Homayoun (2020) assert that companies are increasingly expected to demonstrate a commitment to addressing social concerns and integrating them into their regular operations. Social considerations can have a significant impact on an organization's effectiveness. Companies that prioritize social responsibility are more likely to attract and retain employees who share their values and goals, leading to higher employee satisfaction.

Moreover, socially conscious companies are more likely to attract and retain customers who value ethical behavior by firms (Barauskaite and Streimikiene, 2021). Examples of social aspects include human rights, community involvement, and employment practices. Organizations may establish goals for fair labor practices, implement employee training and development programs to enhance

employee well-being, and create initiatives to foster civic engagement and support charitable causes (Carnevale, 1990).

Recent studies suggest that organizations adopting comprehensive social reporting practices tend to experience improved financial performance. For instance, Zhou et al. (2022) discovered a positive relationship between the quality of social disclosure and firm financial performance, indicating that firms with higher-quality social reports tend to achieve better financial outcomes. Similarly, Khojastehpour and Saleh (2020) demonstrated a positive association between the transparency of social reporting and firm market value.

The impact of contextual factors on the relationship between social reporting and firm performance is noteworthy. Industry characteristics, in particular, play a significant role in shaping this relationship, as evidenced by studies conducted by Nedelcu et al. (2017) and Dima (2018). Sengur (2020) further observed that the positive influence of social reporting on firm value is more pronounced in industries with higher social demands, underscoring the significance of considering industry-specific factors.

Additionally, the relationship between social reporting and firm performance is influenced by regulatory environments and stakeholder pressures. Axjonow et al. (2018) conducted research demonstrating that companies operating in countries with stricter social regulations tend to exhibit a stronger positive association between social reporting and financial performance.

However, it is important to note that conflicting findings also exist. Some studies have discovered either weak or no significant associations between social reporting and firm performance. For instance, Aras and Crowther (2008) found no significant relationship between social reporting and financial performance among Turkish companies. These contrasting results suggest that the relationship between social reporting and firm performance is complex and contingent upon various factors, including industry characteristics, firm size, and stakeholder expectations.

2.3. Governance Factors

Regulations play a significant role in shaping businesses, particularly for new ventures, as highlighted by Trifu et al. (2015). Governance elements encompass the internal rules, practices, and controls that organizations employ to ensure ethical and responsible corporate behavior. Key factors in ensuring openness and accountability include the board of directors, management team, and internal audit division, as indicated by Aksoy et al. (2020).

The effectiveness of a company is greatly influenced by governance factors. Businesses that prioritize excellent corporate governance often achieve greater financial returns by reducing the risk of fraud and financial mismanagement, as noted by Nieschwietz, Schultz Jr, and Zimbelman (2000). Ahammad (2017) further emphasizes that companies practicing ethical and responsible business conduct are more likely to attract and retain investors and clients who value strong corporate governance.

Considering governance concerns is crucial for organizations, as they have a significant impact on performance. According to Landi and Sciarelli (2018), companies that prioritize sound corporate governance are more likely to experience improved financial performance and attract a higher proportion of morally and ethically conscious consumers and investors.

Research suggests that organizations adopting comprehensive governance reporting practices tend to achieve better financial performance. For instance, Xie et al. (2019) found a positive correlation between the quality of governance disclosure and firm financial performance, indicating that firms with higher-quality governance reports tend to achieve superior financial outcomes. Similarly, Ghoul et al. (2017) demonstrated a positive association between transparency in governance reporting and firm value.

Moreover, the practice of governance reporting is associated with increased investor confidence and trust. Adams (2017) conducted research highlighting the positive correlation between governance reporting and investor perceptions of firm value. This suggests that organizations with transparent governance practices are more likely to attract and retain investors, resulting in improved access to capital and investment opportunities.

The relationship between governance reporting and firm performance is influenced by contextual factors. Regulatory environments and institutional factors play a significant role in shaping this relationship. Yang and Babiak (2023) found that the positive impact of governance reporting on firm performance was more pronounced in countries with stronger legal and institutional frameworks, emphasizing the importance of considering country-specific factors. Furthermore, board characteristics and governance structure also influence the relationship between governance reporting and firm performance. Rossi et al. (2021) conducted research showing that board independence and board size moderate the relationship between governance reporting and firm financial performance, highlighting the significance of internal governance mechanisms.

In conclusion, governance considerations have a substantial impact on a company's performance (Arvidsson and Dumay, 2022). Companies that prioritize effective corporate governance often outperform their competitors in terms of financial performance, attract and retain customers, and appeal to investors who value moral and ethical business practices (Aula and Mantere, 2020).

Based on the presented literature review, the following research question arises: Do environmental, social Factors and governance factors have positive associations with financial performance?

3. Methodology

To address the research inquiry, this investigation utilizes a quantitative approach to explore the correlation between Environmental, Social, and Governance (ESG) reporting factors and performance. A sample of 160 companies operating in diverse European countries is selected, and their annual reports serve as the data source. The Statistical Package for the Social Sciences (SPSS) is employed for data analysis. The study adopts a cross-sectional design, examining the selected companies' ESG reporting factors and financial performance during a specific year.

Throughout the research process, ethical considerations are given due attention. The data utilized for analysis is sourced from publicly available annual reports, ensuring compliance with legal and ethical requirements. The confidentiality and anonymity of the companies' data are preserved, and the findings are presented in an aggregated and non-identifiable manner.

4. Findings

The summary of the regression model used to investigate the association between Environmental Factors, Social Factors, Governance Factors, and Financial Performance is provided. The coefficient of determination (R-square) is 0.321, indicating that approximately 32.1% of the variability in Financial Performance can be explained by the independent variables (Environmental Factors, Social Factors, and Governance Factors). The remaining 67.9% of the variability is influenced by other factors not considered in the model. The adjusted R-square is 0.310, which adjusts the R-square value to account for the number of predictors, providing a more conservative estimate of the model's explanatory capacity. The standard error of the estimate is 0.571, representing the average deviation between the actual Financial Performance values and the model's predicted values. A lower value indicates a better fit of the model to the data.

The constant term in the regression equation is 1.213, representing the estimated average Financial Performance when all other independent variables (Environmental Factors, Social Factors, and Governance Factors) are zero. The coefficient for Environmental Factors is 0.269, suggesting that, on average; a one-unit increase in Environmental Factors corresponds to a 0.269 unit increase in Financial Performance, while keeping other variables constant. The coefficient for Social Factors is 0.060, indicating that, on average, a one-unit increase in Social Factors is associated with a 0.060 unit increase in Financial Performance, with other variables held constant. The coefficient for Governance Factors is 0.438, suggesting that, on average; a one-unit increase in Governance Factors is linked to a 0.438 unit increase in Financial Performance, while other variables are kept constant.

These coefficients provide insights into the direction and magnitude of the relationships between the independent variables (Environmental Factors, Social Factors, and Governance Factors) and the dependent variable (Financial Performance). However, it is important to further analyze and interpret the statistical significance and practical implications of these coefficients within the specific context of the research study.

Table 1: Regression Analysis

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.460[a]	.321	.310	.571

a. Predictors: (Constant), Environmental Factors, Social Factors, Governance Factors and Financial Performance

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.213	.089		12.405	.000
	Environmental Factors	.269	.019	.236	12.860	.000
	Social Factors	.060	.018	.045	3.180	.002
	Governance Factors	.438	.020	.391	16.860	.001

a. Dependent Variable: Financial Performance

The strength and significance of the relationships between the variables were assessed using Pearson correlation coefficients. Table 2 presents the correlations between the variables of interest: Environmental Factors, Social Factors, Governance Factors, and Financial Performance. The correlations were evaluated with a significance level of 0.01 in a two-tailed test.

The results indicate several significant correlations between the variables. Firstly, there is a statistically significant positive correlation between Environmental Factors and Financial Performance ($r = 0.251^{**}$, $p < 0.01$). This finding suggests a moderate positive relationship between the extent of environmental considerations and financial performance. Companies that prioritize environmental sustainability tend to exhibit better financial performance.

Secondly, a statistically significant positive correlation is observed between Social Factors and Financial Performance ($r = 0.286^{**}$, $p < 0.01$). This correlation indicates a moderate positive relationship between social responsibility considerations and financial performance. Companies that prioritize social factors, such as employee well-being and community engagement, tend to demonstrate improved financial performance.

Thirdly, a statistically significant positive correlation is found between Governance Factors and Financial Performance (r = 0.219**, $p < 0.01$). This correlation suggests a moderate positive relationship between strong governance practices and financial performance. Organizations with effective governance structures and processes tend to achieve better financial performance outcomes.

These findings provide support for the hypothesis that Environmental Factors, Social Factors, and Governance Factors are positively associated with Financial Performance. However, it is important to note that correlation does not imply causation, and there may be other unmeasured variables that contribute to financial performance.

Table 2: Pearson Correlations

Correlations					
		Environmental Factors	Social Factors	Governance Factors	Financial Performance
Environmental Factors	Pearson Correlation	1	.341**	.408**	.251**
	Sig. (2-tailed)		.000	.000	.000
Social Factors	Pearson Correlation	.341**	1	.373**	.286**
	Sig. (2-tailed)	.000		.000	.000
Governance Factors	Pearson Correlation	.408**	.373**	1	.219**
	Sig. (2-tailed)	.000	.000		.000
Financial Performance	Pearson Correlation	.251**	.286**	.219**	1
	Sig. (2-tailed)	.000	.000	.000	
**. Correlation is significant at the 0.01 level (2-tailed).					

The findings indicate that organizations that prioritize environmental sustainability, social responsibility, and effective governance practices are more likely to achieve better financial performance. These results have implications for practitioners and policymakers, emphasizing the importance of integrating ESG considerations into business strategies to enhance financial performance.

The impact of environmental factors on financial performance is significant. Organizations that incorporate environmental considerations into their strategies and operations can benefit from cost reductions, improved reputation, reduced regulatory risks, access to new markets, and increased investor confidence. Although challenges exist, organizations can address them by adopting a long-term perspective, fostering collaboration, engaging employees, and communicating with stakeholders. By embracing environmental sustainability, organizations not only contribute to a more sustainable future but also enhance their financial performance and create value for all stakeholders.

Social factors play a critical role in shaping organizational success and financial performance. In an interconnected and socially conscious world, organizations are recognizing the importance of social considerations in value creation and the development of sustainable business models. Investments in employee well-being, satisfaction, and development contribute to a positive work environment

and foster employee engagement. Engaged employees are more likely to be motivated, productive, and committed, leading to increased operational efficiency and improved financial performance. Social initiatives such as employee training and development programs, work-life balance initiatives, and employee recognition schemes can have a positive impact on financial outcomes.

Governance factors play a pivotal role in shaping the organization's relationships with its stakeholders, which encompass employees, customers, suppliers, and communities. By prioritizing the interests of these stakeholders, organizations can cultivate trust, foster strong relationships, and enhance their reputation. Positive stakeholder relationships, in turn, contribute to customer loyalty, employee satisfaction, and successful supplier partnerships, all of which have a positive impact on the organization's financial performance.

However, implementing effective governance practices may encounter certain challenges, including resistance to change, a lack of transparency, and a dearth of expertise among board members. To address these challenges, organizations should ensure that their board composition includes directors with diverse backgrounds, expertise, and industry knowledge. This diversity promotes comprehensive decision-making, encourages innovation, and enables effective oversight of the organization's operations. It is also important to establish a robust risk management framework that identifies, assesses, and manages risks. Fostering a culture of risk awareness and providing training to employees at all levels can promote risk mitigation and ethical behavior within the organization.

Transparency is another critical aspect of governance. Organizations should strive to provide comprehensive and timely reporting of both financial and non-financial information to stakeholders. Establishing mechanisms for accountability, such as independent audits and regular performance evaluations, helps ensure compliance and reinforces stakeholder trust. Moreover, nurturing an ethical corporate culture is essential. This can be achieved by setting the tone from the top through ethical leadership. Encouraging ethical behavior, integrity, and adherence to ethical codes of conduct fosters a culture of trust, responsibility, and accountability, which positively influences the organization's financial performance

5. Conclusion

The literature review provides strong evidence of the interdependence of environmental, social, and governance (ESG) factors and their substantial impact on organizational performance. Companies that prioritize environmental sustainability, social responsibility, and good governance attract and retain customers and investors who value ethical business practices.

The literature review also highlights several key themes and patterns regarding the relationship between ESG variables and organizational performance. These include the widespread adoption of initiatives to address ESG elements, a positive correlation between ESG factors and organizational success, and the increasing relevance of ESG factors in decision-making processes.

Empirical research findings confirm that organizations with strong ESG performance tend to achieve better financial outcomes. This indicates that investors and financial markets recognize the

value of sustainable business practices and consider ESG factors when making investment decisions.

ESG reporting factors contribute to operational efficiency by enabling organizations to measure and disclose environmental and social performance metrics. This allows them to identify areas for improvement, implement sustainable practices, and optimize operational processes, resulting in cost reductions, resource efficiency, and improved risk management.

ESG reporting also plays a crucial role in building and maintaining a positive corporate reputation. Transparent communication of ESG initiatives and performance fosters trust and credibility among stakeholders, leading to increased customer loyalty, enhanced brand value, and improved stakeholder engagement. Demonstrating a commitment to responsible and sustainable practices is increasingly important to consumers, employees, investors, and communities

As the significance of sustainable business practices continues to grow, organizations need to recognize the value of ESG reporting and its impact on performance. By adopting robust ESG reporting practices, organizations can meet stakeholder expectations, seize opportunities for innovation and risk mitigation, and create long-term value.

To gain a deeper understanding of the relationship between ESG factors and business success, future research could consider qualitative methods such as comprehensive case studies. Additionally, it would be beneficial to include a broader spectrum of businesses, including small and medium-sized enterprises (SMEs), for a more comprehensive view of the effect of ESG issues on organizational performance.

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