

Does Institutional Quality and Managerial Ability Drive the Association between ESG and Firm Performance: Evidence from Emerging Asian Markets

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Abstract

This study aims to explore the role of managerial ability (MA) and institutional quality (IQ) in enhancing the positive impact of Environmental, Social, and Governance (ESG) policies on financial performance (FP). Against the backdrop of global climate change, socio-economic advancements, and evolving corporate governance standards, organizations face increasing pressure to adopt ESG practices. However, the implementation of ESG policies often entails substantial costs. By investigating the joint influence of MA and IQ, this research seeks to identify supplementary factors that can amplify the beneficial effects of ESG initiatives on FP. The study is quantitative exploratory and uses panel data of 750 publicly listed companies covering period from 2010 to 2020. Data has been acquired from the reputed data provider like Thomson Reuters and OLS regression has been used for panel data analysis. Two measures of financial performance, the Tobin's Q and Return of Assets (ROA) have been used as proxies of financial performance. The study reaffirms the positive impact of Environmental, Social, and Governance (ESG) factors on the financial performance of firms. Each pillar of ESG – environmental, social, and governance – is positively correlated with financial performance. Additionally, managerial ability and institutional quality act as supplementary variables, moderating the relationship between ESG and firms' financial performance. Notably, both proxies of financial performance, Tobin's Q and Return on Assets (ROA), yield nearly identical results in terms of their relationships with ESG and the moderating effects of managerial ability and institutional quality. Data of only 750 firms used for the analysis. Latest data was not available, therefore, data from 2010 to 2020 was used in the study. The study underscores the potential for inducing Environmental, Social, and Governance (ESG) practices in emerging economies through a combination of managerial ability and institutional pressures. It emphasizes the role of policymakers in addressing inefficiencies, corrupt practices, and policy inconsistencies that impede the governance index and hinder the ease of doing business. At the organizational level, policymakers should prioritize appointing managers with higher managerial ability to responsible positions. For managers, understanding the long-term benefits associated with ESG practices is crucial, despite potential short-term challenges. While previous research often focused on specific countries, regions, or industries, this study stands out by examining the relationship between ESG and FP across multiple emerging economies and industries, offering more generalizable findings. Building upon Stakeholders' Theory, the study extends Upper Echelon Theory and Institutional Theory to incorporate the roles of managerial ability and institutional quality in shaping this relationship."

Keywords – Environmental, Social, Governance, , ESG, Institutional Quality, Managerial Ability, Financial Performance.

Introduction

The combination of environmental dangers, ineffective governance, and a lack of awareness within society has resulted in catastrophic consequences for the populace, causing significant harm to ordinary citizens. Recently,

the United Nations Organization outlined a set of 17 sustainable development goals (UNO, 2023). As per UN guidance, every member state is required to integrate these SDGs across all sectors of society within its borders by the year 2030. In the corporate world, businesses, as prominent entities, cannot ignore their responsibilities within their respective countries (Rosati et al., 2023). Consequently, they are actively working to meet public needs and address demands for social welfare (Galeazzo, Miandar, & Carraro, 2023). To stay in line with societal expectations and ethical standards, forward-thinking organizations must adopt environmental, social, and governance (ESG) practices (Irfan, Bhatti, & Ozturk, 2021). This broader set of responsibilities is encompassed within the concept of ESG, which is integrated into the larger framework of sustainability (Dalal & Thaker, 2019). Companies are now assessed not only on their profitability but also on their efforts toward environmental preservation, community development, and improved corporate governance (Chen, Song & Gao, 2023). Additionally, besides the benefits to reputation, the focus on ESG by firms in Emerging Markets of Asia seems to be motivated by expected enhancements in financial performance (FP), facilitating business growth and entry into new markets.

Previous research predominantly supports the positive impact of firms adopting ESG practices and highlights the likelihood of improved FP resulting from increased ESG engagement (Chen et al., 2023). Additionally, it has been noted that ESG strategies are linked to managers' inherent ability and past experience termed as Managerial ability (MA) to formulate and implement strategies, decisions, and future plans (Chatjuthamard, Jiraporn, Tong & Singh, 2016; Yuan, Tian, Lu, & Yu, 2017). Hermalin and Weisbach (2017) suggest that key stakeholders such as financiers, financial analysts, and customers continuously evaluate the Managerial ability of top management by observing their approach, intentions, competence, and personalities, which ultimately influence their interests. In addition to Managerial ability, another significant factor influencing the adoption of ESG practices is the institutional quality (IQ) of a country. IQ encompasses various factors that facilitate the exercise of authority within a nation, including political stability (Glaeser et al., 2004), the legal environment (La Porta et al., 2006), and regulatory quality (Djankov et al., 2002). IQ creates a supportive environment for business activities and moderates the potential impact of ESG on FP (Pinheiro, Santos, Cherobim & Segatto, 2023). A higher IQ assures investors, customers, and other stakeholders that they are protected by the law in their endeavors, and their rights and investments in human and physical capital are secure (Yuan et al., 2017).

This study suggests that in environments with higher institutional quality (IQ), organizations with stronger managerial ability (MA) can improve their financial performance (FP) by adopting ESG practices. The conceptualization of the relationships among IQ, MA, ESG, and firms' FP is rooted in the rationale proposed by the upper echelon theory (Hambrick & Mason, 1984) and institutional theory (Scott, 1987). According to these theories, organizational leaders with better MA, operating within a context of higher institutional quality, are more inclined to prioritize the interests of stakeholders. Existing literature indicates that IQ tends to be more stable and robust in developed markets, whereas in emerging economies, it is lower and subject to fluctuations. (Bibi, Butt, & Awais, 2024; Nasir, Awais, & Syed, 2017). This discrepancy is largely attributed to factors such as higher levels of corruption, inconsistent policies, weak governance, limited regulatory oversight, and lower adherence to the rule of law (Abaidoo & Agyapong, 2021).

Firms characterized by higher institutional quality and stronger managerial ability are inclined to support ESG initiatives, leading to improved FP (DasGupta, 2022). To explore the combined effects of institutional quality (IQ) and managerial ability (MA) on FP through ESG practices, a moderated moderation (double moderation) methodology has been employed. Therefore, further research is needed to understand the interplay between MA at the firm level and IQ at the country level and their role in shaping the relationship between ESG and FP (McWilliams & Siegel, 2001). For academia, this research has great significance in view of its methodology which is dual moderation (moderated moderation) method in understanding the ESG and FP relationship. This new methodology gives a new framework to researchers, who can check this by using other ESG related variables. These variables can also be tested for other regions / sectors in order to achieve generalizable findings. This study marks the first of its kind effort which examine the moderating effect of managerial ability reinforced by institutional quality on the relationship between ESG and FP.

Literature Review and Hypotheses Development

Theoretical Review

The three explanatory variables ESG, MA and IQ explained in this paper are based on Stakeholders, Upper echelon and Institutional theories respectively. The stakeholder perspective underpins the relationship between ESG and FP organizations. Tantalo and Priem (2016) argue that different stakeholders, such as investors, creditors, employees, customers, and regulators, view ESG as potential drivers of value creation. Managing key business and stakeholder relationships is critical to FP development. According to Harman et al. (2010). By engaging in social and environmental leadership and following good leadership practices, companies can delight their stakeholders and thus improve FP (Aboud & Diab, 2018). Upper Echelon theory provides a framework for understanding how the characteristics of top managers affect firm performance. The theory suggests that top managers' unique characteristics, world economic history, and financial values influence their choices and organizational outcomes. Therefore, senior managers' private views can influence their decision-making and subsequent performance outcomes. Research by Reinmoeller (2004) and Hambrick (2007) highlighted the impact of managerial behavior on the decision-making process. ESG (environmental, social, governance) measures represent strategic choices and therefore influence management. Most ESG practices reflect broader direction from senior management, and senior management behaviors are more likely to influence ESG measures. According to DiMaggio and Powell (1983), the Institutional theory posits that organizations adopt business practices to bolster their legitimacy. This theory aims to clarify the reasons behind nations' dedication to sustainable institutional frameworks and the various shapes these frameworks assume. Institutional theory, as outlined by DiMaggio and Powell (1983), places significant emphasis on how organizations establish and sustain legitimacy by embracing widely accepted structures and practices, termed as isomorphism. Although institutions are typically more robust in developed nations, they often lag behind in emerging economies.

ESG and Financial Performance of Firms

Extant literature indicates that firms following ESG protocols and actively pursuing ESG implementation may or may not muster higher FP (Lee & Suh, 2022). Friede et al. (2015) analyzed almost 2000 studies and found a positive link between ESG – FP relationship in most of the cases. Aboud & Diab (2018) emphasized that due to pressure from stakeholders on firms to disclose their ESG activities, a positive link was discovered between ESG and FP. At the same time, it is argued that ESG investment reduces the opportunities to exploit resources to maximize profit as it involves higher costs, thereby increasing the conflict of interest among stakeholders (Barnett, 2007), which triggers competitive disadvantages and eventually diminishes firms' FP (Ahmad et al., 2021). In the case of developed markets, the studies mostly found a strong correlation between ESG and firms' FP, while in the case of emerging economies, mixed results were obtained (Bahadori, Kaymak, & Seraj, 2021). Covering emerging economies, Shakil et al. (2019) revealed the positive impact of ESG on firms FP, while Atan et al. (2018) found insignificant effects. Park's (2017) survey of 175 emerging Korean firms between 2010 and 2012 shows that ESG has a positive effect on long-term firm performance and provides direct and indirect value to firms through positive reputational feedback. In an emerging market like Malaysia, creating value by integrating ESG into a firm's long-term strategy with the right vision will attract the best talent, acquire authentic customers through an effective management structure, and increase shareholder value. In Taiwan, Wu et al. (2014) found that high CSR disclosure is associated with lower capital costs as a result of financial institutions recognizing firms' efforts to improve sustainability. Buallay (2019) examines firms in developing and emerging markets and finds mixed results on the impact of ESG on performance. Environmental disclosure has a positive effect on performance, while a negative relationship was found between corporate social responsibility disclosure and performance. Park's (2017) survey of 175 emerging Korean firms between 2010 and 2012 shows that ESG has a positive effect on long-term firm performance and provides direct and indirect value to firms through positive reputational feedback. In an emerging market like Malaysia, creating value by integrating ESG into a firm's long-term strategy with the right vision will attract the best talent, acquire authentic customers through an effective management structure, and increase shareholder value. In Taiwan, Wu et al. (2014) found that high CSR disclosure is associated with lower capital costs as a result of financial institutions recognizing firms' efforts to improve sustainability. Conversely, Jo et al. (2015) found that ESG costs adversely affect a firm's FP. In a highly competitive market, disclosure of ESG information will facilitate a firm's trust and ability to generate better performance compared to its competitors and motivate firms to actively engage in higher ESG activities to meet

market expectations (Li et al., 2018). Besides a few negative and inconclusive results, most of the studies found a positive and significant relationship between ESG and firms' FP. Hence, the paper hypothesize:

Hypothesis-1: *There is a positive relationship between ESG performance and Firms' FP in Asian Emerging Markets.*

ESG and firm FP: The Moderating role of Managerial Ability (MA)

The lack of consensus on the ESG-FP relationship seems due to theoretical and empirical limitations, among which is the lack of consideration of other variables at the firm and country level (McWilliams & Siegel, 2001). In this context, the MA at the firm level is an important variable that can further explain the ESG-FP relationship. It is expected that managers having better MA manage firm's resources more efficiently, that minimize costs and maximize benefits from ESG related projects for better financial gains. This indicates that higher MA acts as a guarantor of the benefits of ESG in firms (Gong, Yan, & Ho, 2020). However, managers having low MA might show lesser enthusiasm for ESG projects as they focus on short-term investments, avoiding risky and uncertain projects that generate career concerns for them (Lee, Wang, Chiu, & Tien, 2018). Whereas in case of managers with higher MA, they may undertake ESG actions to garner the support and satisfaction of various stakeholders that will benefit their organizations. ESG has become an important aspect of business, attracting global attention from CEOs (Fabrizi et al., 2014). CEOs recognize that neglecting to invest in ESG efforts can lead to negative publicity and public relations. Additionally, consumers have expressed interest in limiting the products and services offered by companies that do not prioritize ESG consideration. Daradkeh et al. (2022) suggested that higher MA focus on activities that require continuing commitments that are beneficial to a broader spectrum of investors. García-Sánchez and Martínez-Ferrero (2019) argued that the ablest CEOs allocate the available resources to ESG more efficiently and enhance firm value. On the contrary, excessive ESG activities may cause firms to experience losses, if they are not purely profitability-oriented. Consequently, a negative association between ESG and firms' FP might be observed in this case. ESG can be used by managers as a tool to further their interests, which could negate the interests of shareholders. The strength of the corporate governance mechanisms in place would serve to prevent or promote the achievement of individualistic interests of managers in the use of CSR decisions. This therefore shows that the financial result (profitability) of ESG activities and related disclosures can be affected by the nature and effectiveness of the governance mechanisms applied by top management that exist in the organization. Building upon the upper echelon theory, Chatjuthamard et al. (2016) and Yuan et al. (2017) linked MA with their ESG performance and suggested a positive outcome. Hence, based on these considerations, the following hypothesis is formed:

Hypothesis-2: *The Managerial ability moderates the relationship between ESG and Firms' FP in Asian Emerging Markets.*

ESG and Firm FP: Moderating role of Institutional Quality (IQ)

In line with previous studies, a positive link between ESG and FP enables us to extend the argument further to include IQ as a country-level moderating variable in the said relationship. IQ is defined as a set of factors that collectively form rules and constraints to be adhered to by a country at the macro level, it shapes the economic behavior and contribute towards economic development (Ortas et al., 2015). Since ESG still relies on the voluntary initiatives of the reporting entity, in the absence of any mandatory requirement, with a weak institution and a lack of laws, companies operating in this kind of environment are likely to benefit from a poor governance system. by not emphasizing disclosure. It is against this background that we consider it necessary to examine the financial performance implications of firms that choose to look beyond the system's weaknesses and do what is right. Extent literature while analyzing the impact of IQ on a firm's financial performance shows significant and positive results. Nations with weak rule of law and governance structures may exhibit less competitive and weaker firms (Klomp & De Haan, 2015). Various institutional factors, alongside organizational considerations, motivate management to integrate strategies that cater to both stakeholders and shareholders (El Ghouli et al., 2017). Past literature reviews underscore differences in institutional contexts between advanced and emerging economies, particularly regarding attributes such as government stability, effectiveness, accountability, control over corruption (Cheng et al., 2014), and regulatory frameworks (Ioannou and Serafeim, 2014). These disparities in academic research across countries, as noted by Jamali and Karam (2016), are inherently contextual and

influenced by multifaceted factors and actors within broader formal and informal governance systems. The institutional context can significantly influence the determination of suitable ESG priorities and initiatives (Hamann, 2006; Visser, 2005), which consequently have varying impacts on financial performance. The theoretical rationale behind these varying effects may lie in the governance pillar, which appears highly influenced by the overall governance environment of the country. Phan et al. (2021) found in their research that ESG performance and oil price uncertainty are negatively related, while country-level institutional quality moderates and further strengthens the negative relationship between ESG and oil price uncertainty. Hunjra et al. (2020) when investigating the moderating role of institutional quality (measured only by the corruption factor) on the link between the environmental component of ESG and financial development, found positive and significant results. Karmani and Boussaada (2021) found that the effect of ESG in the presence of better institutional quality significantly enhance firms' FP. Likewise, in case of emerging economies, Alam and Yazdifar (2019) explored that the IQ of a country was positively related to the FP of firms. Despite few insignificant results, generally the outcome remains significant. Liu et al. (2022) also examined the moderating role of IQ on ESG and firm's FP and found a positive outcome. Hence, based on these research findings, the following hypothesis was formed:

Hypothesis-3: *The IQ moderates the relationship between ESG and Firms' FP in Asian Emerging Markets.*

ESG and firm FP: Double Moderation by MA and IQ

After having established the possibility a moderating role of managerial ability on the relationship between ESG and firms' FP, it is likely that this relationship is influenced by the country's institutional quality state. Very little literature is found in this context, while some is found in bits and pieces. In consonance with the Stakeholders Theory and Upper Echelon Theory, MA moderates the ESG-FP relationship. The ESG-FP relationship is further influenced by macro level variables such as IQ, that considerably affects MA and top management's decision-making process (Krasniqi & Mustafa, 2016). Among the many factors considered to influence firm productivity in emerging markets, institutional quality is a determinant of firm performance (Dollar, Hallward-Driemier, & Mengistae, 2005; Lu, Png, & Tao, 2013). Institutional failure can lead to ecosystem degradation. Well-functioning quality institutions improve the environment even if the country has a low level of income. With higher IQ elements, the firms find conducive environments to undertake ESG initiatives. In case of a low IQ index, the MA of firms will be affected that restrict management from undertaking long-term ESG projects. Ortas et al. (2015) argued that ESG performance is affected due to divergent behaviors of managers under similar institutional backgrounds. Whereas, able managers are expected to evaluate the prevailing ESG protocols better and manifested consistency under varied IQ environments (Inam et al., 2021). Under weak IQ level, firms' management is poised to invest in projects that are risky but could improve managerial power or prestige, as against those that increase payouts to shareholders and improve firm value (Fahlenbrach, 2009). A better MA entails that the able managers used their specific knowledge and experience for better evaluations of ESG activities even in unfavorable institutional environments. Therefore, it is expected that in varying IQ environments, good MA might promote more ESG application than low MA. According to Zhao et al. (2018) investors consider ESG activities along with institutional quality when analyzing emerging markets in order to better understand the external governance environment prevailing within (Aboud & Diab, 2019). Based on these considerations, the following hypothesis is framed:

Hypothesis-4: *The relationship between ESG and Firms FP moderated by MA is reinforced by IQ in Asian Emerging Markets.*

Methodology

Sample and Data Description

The sample comprising 750 Publicly Listed Companies from 13 Emerging Asian Economies i.e., China, Russia, India, Indonesia, South Korea, Malaysia, Philippines, Taiwan, Thailand, Singapore, Hong Kong, Turkey, and Pakistan. These countries were considered emerging economies by renowned organizations like the IMF (IMF, 2021), World Bank (WB, 2021), and Michigan Studies University (MSU-CIBER, 2020). These markets are also considered because of their membership in various emerging economic blocks like EAGLE, N-11, and BRICS (Sultanuzzaman et al., 2019). Within each country, only those firms were selected which were listed in the

respective stock exchanges and regularly reported ESG data for the last eleven years (2010-2020). The data for this study were obtained from Thomson Reuters Eikon for ESG, FP, MA, and control variables whereas for IQ the data is extracted from WGI (Worldwide Governance Index by World Bank) covering a period of analysis from 2010 to 2020. After excluding observations without financial data, MA, and ESG data, a final unbalanced sample of 8400 firm-year observations spanning 11 years was available to test the hypotheses. The selected 750 firms were engaged in businesses in different sectors like manufacturing, financial services, and utilities. Details of firms is as under:

Sector-Wise Distribution of Firms

Manufacturing	Services	Total
348	402	750

Variables of the Study and their Measurement

ESG performance. For this study, ESG scores data of 13 Asian Emerging economies were extracted from Thomson Reuters Refinitiv Eikon DataStream formerly known as Asset 4. This DataStream is a reliable and well-known database for providing comprehensive ESG and financial information. It releases the ESG rating scores and other relevant data yearly. The sample is chosen based on the availability of firms' ESG score which ranges from 0-100. The ESG index comprising three pillars i.e., Environment, Social, and Governance. The pillars are further divided into ten categories. Environmental pillar has three categories i.e., resource use, emissions, and innovations. Social pillar had four categories i.e., workforce, human rights, community, and product responsibility. There were three categories of the governance pillar which included management, shareholders, and CSR strategies. The categories were measured through 70 indicators/key performance indicators (KPIs).

Managerial Ability. Managerial ability (MA) is measured by using the residual-based model proposed by Demerjian et al. (2012) to assess management proficiency. He used two-step approach to quantify MA by using the data envelopment analysis (DEA) method. Firstly, the firms' efficiency was estimated by examining the allocation of corporate resources versus net sales or revenue. Secondly, using a Tobit regression, the predicted efficiency scores were correlated with firm attributes. The remaining unexplained variables were indicative of management skill after controlling for firm factors and efficiency (Demerjian et al. 2012). In this study, main indicators were allocated resources of the firm (cost of doing business) and the revenue generated from these resources (revenue earned). The efficiency ratio (ratio between the utilized resources of the firm and the revenue earned) indicated the MA.

Institutional Quality (IQ). This study used IQ data as formulated and compiled by the World Bank (Worldwide Governance Index). This database provided comprehensive, updated, and wide coverage data in terms of timeframe and incorporated a larger number of countries than other governance indexes (Sharma & Paramati, 2021). The indicators used for measurement of IQ by the world bank included control of corruption, government effectiveness, political stability and absence of violence, voice and accountability, regulatory quality and rule of law.

Firm's Financial Performance. To measure the FP of firms, two proxies were used to measure firms' FP i.e., ROA and Tobin's Q. ROA showed the efficiency of use of the firm's assets, it is the accounting measure reflecting its operational performance and is widely used in past studies in the context of the ESG-FP relationship (Khoury et al., 2021). "Tobin's Q" was calculated by the sum of the market value of equity plus short-term debt plus long-term debt divided by total assets (Chung & Pruitt, 1994). The calculated ratio was an indicator of the perception about the company by people in the market place and stock exchange.

Control variables. In addition, to avoid biased results in our proposed models, we included several control variables (firm, and country-level aspects) as used in previous studies on ESG and firm FP relationship. The firm-level control variables included "Size" as the natural logarithm of total assets, "Leverage" as the ratio of total debt to total assets, "Age" as the number of years passed starting from its origin till 2020, "Sales" as the ratio of sales to total assets and "Cash" as the ratio of cash holdings to total assets. The country-level control variable included "GDP Growth" that is the change in the GDP from consecutive years and based on market prices at local currency.

Finally, to control for variation across time, country, and industry; the dummies for year, country, and industry were included.

Model and Analysis Technique

The econometric models were created by the authors of this study based on review of the literature to analyze panel data using regressions with the Ordinary Least Square (OLS) estimation technique. OLS was used for this study because the aim was to investigate the relationship between ESG and financial performance of firms. For focusing on the said relation, it was assumed that the individual differences of firms were uniform. There was no intention of exploring the individual differences of the firms, countries, or business sectors which would be attempted in future studies by authors using fixed and/or random effects models. For H-1 the “ROA” and “Tobin Q” were regressed on ESG along with the control variables. To support Hypotheses 1 (H1), we expected a positive and significant coefficient for the ESG in line with the following equations:

$$ROA_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 Size_{i,t} + \beta_3 Age_{i,t} + \beta_4 leverage_{i,t} + \beta_5 GDPgrowth_{i,t} + \beta_6 Sales_{i,t} + \beta_7 Cash_{i,t} + \beta_8 Year_{i,t} + \beta_9 Industry_{i,t} + \beta_{10} Country_{i,t} + \varepsilon_{i,t} \quad (1)$$

$$Tobin's\ q_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 Size_{i,t} + \beta_3 Age_{i,t} + \beta_4 leverage_{i,t} + \beta_5 GDPgrowth_{i,t} + \beta_6 Sales_{i,t} + \beta_7 Cash_{i,t} + \beta_8 Year_{i,t} + \beta_9 Industry_{i,t} + \beta_{10} Country_{i,t} + \varepsilon_{i,t} \quad (2)$$

Where i = indicates a specific firm; t = indicates a specific fiscal year and ε = random disturbance term.

To test Hypothesis 2 (H2), MA and its interaction term with ESG were added along with the control variable:

$$ROA_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 (ESG * MA)_{i,t} + \beta_3 MA_{i,t} + \beta_4 Size_{i,t} + \beta_5 Age_{i,t} + \beta_6 leverage_{i,t} + \beta_7 GDPgrowth_{i,t} + \beta_8 Sales_{i,t} + \beta_9 Cash_{i,t} + \beta_{10} Year_{i,t} + \beta_{11} Industry_{i,t} + \beta_{12} Country_{i,t} + \varepsilon_{i,t} \quad (3)$$

$$Tobin\ q_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 (ESG * MA)_{i,t} + \beta_3 MA_{i,t} + \beta_4 Size_{i,t} + \beta_5 Age_{i,t} + \beta_6 leverage_{i,t} + \beta_7 GDPgrowth_{i,t} + \beta_8 Sales_{i,t} + \beta_9 Cash_{i,t} + \beta_{10} Year_{i,t} + \beta_{11} Industry_{i,t} + \beta_{12} Country_{i,t} + \varepsilon_{i,t} \quad (4)$$

For testing Hypothesis 3 (H3), IQ and its interaction term with ESG were added along with control variables:

$$ROA_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 (ESG * IQ)_{i,t} + \beta_3 IQ_{i,t} + \beta_4 Size_{i,t} + \beta_5 Age_{i,t} + \beta_6 leverage_{i,t} + \beta_7 GDPgrowth_{i,t} + \beta_8 Sales_{i,t} + \beta_9 Cash_{i,t} + \beta_{10} Year_{i,t} + \beta_{11} Industry_{i,t} + \beta_{12} Country_{i,t} + \varepsilon_{i,t} \quad (5)$$

$$Tobin\ q_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 (ESG * IQ)_{i,t} + \beta_3 IQ_{i,t} + \beta_4 Size_{i,t} + \beta_5 Age_{i,t} + \beta_6 leverage_{i,t} + \beta_7 GDPgrowth_{i,t} + \beta_8 Sales_{i,t} + \beta_9 Cash_{i,t} + \beta_{10} Year_{i,t} + \beta_{11} Industry_{i,t} + \beta_{12} Country_{i,t} + \varepsilon_{i,t} \quad (6)$$

To test Hypothesis 4 (H4), MA and IQ and their interaction terms with ESG were added along with control variables. This hypothesis combines firm specific variable (MA) and the country specific variable (IQ) because of the anticipation of hierarchal moderation effect of IQ on MA and then on the relationship between ESG and financial performance of firms (ROA and Tobin’s Q). The hierarchal moderation by combining different levels of moderating variables is in line with studies by Gajenderan, Nawaz, Rangarajan, and Parayitam (2023); Anurag, Patel, and Parayitam (2023); and Wills et al. (2013). The resultant model is depicted by following equation:

$$ROA_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 (ESG * MA * IQ)_{i,t} + \beta_3 IQ_{i,t} + \beta_4 Size_{i,t} + \beta_5 Age_{i,t} + \beta_6 leverage_{i,t} + \beta_7 GDPgrowth_{i,t} + \beta_8 Sales_{i,t} + \beta_9 Cash_{i,t} + \beta_{10} Year_{i,t} + \beta_{11} Industry_{i,t} + \beta_{12} Country_{i,t} + \varepsilon_{i,t} \quad (7)$$

$$Tobin\ q_{i,t} = \alpha_i + \beta_1 ESG_{i,t} + \beta_2 (ESG * MA * IQ)_{i,t} + \beta_3 IQ_{i,t} + \beta_4 Size_{i,t} + \beta_5 Age_{i,t} + \beta_6 leverage_{i,t} + \beta_7 GDPgrowth_{i,t} + \beta_8 Sales_{i,t} + \beta_9 Cash_{i,t} + \beta_{10} Year_{i,t} + \beta_{11} Industry_{i,t} + \beta_{12} Country_{i,t} + \varepsilon_{i,t} \quad (8)$$

Findings of the Study

Descriptive Results

Table 1 presents the descriptive statistics for the independent variable ESG along with its three pillars; ENV (environmental), SOC (social), and GOV (governance); two moderating variables, MA and IQ, the dependent variable FP (measured by ROA and Tobin’s Q) and six control variables. The value for ESG, which is score from 1 to 100, minimum value was 1.19, representing those firms that were weak in their ESG performance and maximum score was 92.51 showing firms with exceptional ESG-related practices. The mean score for ESG was 41.80, indicating that on average, the sample firms were considerably good in ESG. Similarly, the pillars of ESG

were also scores ranging from 1 to 100. MA was the ratio between allocated resources of the firm and revenue generated from it ranging from 0 to 1. IQ was a score ranging from 1 to 100 whereas the FP, in both cases (ROA and Tobin’s Q) was a ratio. With regard to control variables, firm “Size” was the natural logarithm of total assets, “Leverage” the ratio of total debt to total assets, “Age” as the number of years passed starting from its origin till 2020, “Sales” as the ratio of sales to total assets and “Cash” as the ratio of cash holdings to total assets. GDP was GDP growth calculated as difference between current year with previous year GDP.

Table 1

Descriptive Statistics

Variable	Observations	Mean	Std. Dev.	Min	Max
ROA	8398	.054	.069	-.353	.435
Tobin’s Q	8272	1.182	1.541	.029	26.302
ESG	8448	41.803	20.67	1.19	92.51
ENV	8448	37.525	25.619	.09	98.39
SOC	8448	40.112	25.098	.05	97.25
GOV	8437	50.111	22.302	.6	97.69
MA	8448	.547	.356	.001	.988
IQ	8448	.377	.796	-1.184	1.636
SIZE	8398	18.936	2.656	12.108	27.893
SALES	8398	.656	.577	.015	8.462
CASH	8398	.172	.142	.003	.75
AGE	8448	26.297	16.733	24	73
GDP	8448	2.222	3.405	-14.4	13.395

Correlation Analysis

Correlation analysis revealed that without inclusion of interaction variables (created for checking moderation effects), ESG was found to correlate significantly with financial performance (both ROA and Tobin’s Q). The pillars of ESG were also significantly correlated with ROA and Tobin’s Q. After addition of interaction term (ESG*MA*IQ), the correlation of ESG and its pillars was still significant with ROA and Tobin’s Q while the interaction variable was also significantly correlated with both measures of financial performance. Similarly, the interaction variables of individual pillars of ESG (ENV*IQ*MA, SOC*IQ*MA, and GOV*IQ*MA) were also found significantly correlated with ROA and Tobin’s Q. It was worth noting that the correlation of ESG and its pillars did not change much with addition of the interaction variables. To avoid duplication of similar data without much insight, Table-2 presents only the correlations between variables of model-1 and 2 (without moderation) and model-7 and 8 (with dual moderation).

Table 2
Correlation Table

Variables	(1) ROA	(2) Tobin's Q	(3) ESG	(4) ENV	(5) SOC	(6) GOV	(7) LVG	(8) SIZE	(9) SALES	(10) CASH	(11) Age	(12) GDP
(1) ROA	1.00 (0.000)											
(2) Tobin's Q	0.577* (0.000)	1.000										
(3) ESG	0.043* (0.000)	0.059* (0.000)	1.000									
(4) ENV	0.076* (0.000)	0.119* (0.000)	0.780* (0.000)	1.000								
(5) SOC	0.018 (0.091)	0.038* (0.001)	0.908* (0.000)	0.688* (0.000)	1.000							
(6) GOV	0.023* (0.034)	0.008 (0.487)	0.527* (0.000)	0.270* (0.000)	0.315* (0.000)	1.000						
(7) LVG	- 0.179* (0.000)	-0.145* (0.000)	0.209* (0.000)	0.193* (0.000)	0.202* (0.000)	0.077* (0.000)	1.000					
(8) SIZE	- 0.170* (0.000)	-0.238* (0.000)	0.256* (0.000)	0.226* (0.000)	0.259* (0.000)	0.063* (0.000)	0.066* (0.000)	1.000				
(9) SALES	0.304* (0.000)	0.335* (0.000)	-0.005 (0.621)	-0.007 (0.526)	-0.006 (0.571)	0.005 (0.618)	- 0.083* (0.000)	-0.159* (0.000)	1.000			
(10) CASH	0.268* (0.000)	0.221* (0.000)	- 0.093* (0.000)	- 0.098* (0.000)	- 0.104* (0.000)	-0.011 (0.310)	- 0.102* (0.000)	-0.304* (0.000)	0.082* (0.000)	1.000		
(11) AGE	- 0.023* (0.036)	-0.043* (0.000)	0.150* (0.000)	0.156* (0.000)	0.195* (0.000)	- 0.066* (0.000)	- 0.086* (0.000)	0.267* (0.000)	-0.018 (0.098)	- 0.139* (0.000)	1.000	
(12) GDP	0.097* (0.000)	0.140* (0.000)	- 0.070* (0.000)	- 0.098* (0.000)	- 0.035* (0.001)	- 0.036* (0.001)	- 0.412* (0.000)	-0.038* (0.001)	0.027* (0.013)	- 0.036* (0.001)	- 0.042* (0.000)	1.000

Multivariate Results

The results of the multivariate analysis are explained in the ensuing paragraphs.

Impact of ESG on FP

Two separate regressions were run, firstly the regression of ESG on ROA and Tobin's Q, and secondly the regression of each pillar of ESG (ENV, SOC, and GOV) on ROA and Tobin's Q. The first regression was to verify the positive impact of ESG on financial performance of firms. The purpose of second regression was to determine which of the pillars had the strongest relation with ROA and Tobin's Q. Table 3 presents the results of the multivariate analysis examination of the impact of ESG and its three pillars (ENV, SOC, and GOV) on FP (measured by ROA and Tobin's Q). The effect of ESG on ROA was found positive ($\beta_1 = 0.018$) and significant ($t = 5.238$) at $p < 0.01$ implying that ESG significantly contributes to ROA (firm accounting performance). Individually, the effect of ENV on ROA was positive ($\beta_2 = 0.010$) and significant ($t = 3.721$) at $p < 0.01$ and SOC was also positive ($\beta_3 = 0.018$) and significant ($t = 6.054$) at $p < 0.01$. However, the effect of GOV on ROA was positive ($\beta_4 = 0.005$) but insignificant, which implied that the Governance dimension of ESG was less likely to enhance FP. The result indicated that environmental and social aspects of ESG are being given more attention as compared to governance by the firms in the sampled countries. Likewise, the effect of ESG on Tobin's Q was positive ($\beta_1 = 0.607$) and significant ($t = 8.53$) at $p < 0.01$. Similarly, each pillar of ESG positively contributed to Tobin's Q. The effect of ENV on Tobin's Q was ($\beta_2 = 0.346$) and significant ($t = 6.082$) at $p < 0.01$, SOC on Tobin's Q positive ($\beta_3 = 0.545$), and GOV on Tobin's Q also positive ($\beta_3 = 0.229$) and significant ($t = 3.720$) at $p < 0.01$.

The regression coefficients of the control variables were mostly in consonance with previous studies. The regression coefficients displaying the impact of "Leverage", "Age", "Cash", and "Sales" were positive and significant with ESG. The "Size" had a negative but significant association with ESG which is not consistent with

previous literature. Probably bigger firms do not consider spending more on ESG activities as they have other means to influence the ISOs and other agencies. “GDP” Growth showed a negative and insignificant result, depicting that macroeconomic indicator GDP growth does not affect the ESG activities of firms. This study has found that ESG impacted significantly the firm’s financial performance as determined through both proxies i.e., ROA and Tobin’s Q in Asian emerging economies. The sensitivity of firms towards ESG has been found by other studies to vary considerably from firm to firm and the tendency of disclosure of ESG engagements and outcomes was also found comparatively less prevalent in Asian emerging economies. However, the data analysis in this study explained that the firms that had the inclination to adopt ESG had better financial performance. This evidence was in line with the Stakeholders’ Theory (Freeman, 1984) which declared that trustworthy and strong relationships with stakeholders could be built by firms through ESG-supportive initiatives.

Table 3**Results of Regression Analysis (regression coefficients, significance, and ‘t’ values)**

Variable	ROA	Tobin’s Q
ESG	0.018*** (5.238)	0.607*** (8.533)
ENV	0.010*** (3.721)	0.346*** (6.082)
SOC	0.018*** (6.054)	0.545*** (9.109)
GOV	0.005 (1.581)	0.229*** (3.720)
Lev	0.055*** (8.845)	2.369*** (18.536)
Size	-0.004*** (6.109)	-0.313*** (25.752)
Sales	0.030*** (20.734)	0.667*** (22.454)
Cash	0.112*** (19.709)	1.605*** (13.669)
Age	0.007 (0.666)	0.003*** (2.731)
GDP	-0.001 (-2.013)	-0.007 (-1.219)
Industry Dummy	Yes	Yes
Year Dummy	Yes	Yes
Country Dummy	Yes	Yes
Constant	0.067*** (3.250)	6.027*** (14.096)
Observations	8,272	8,272
R-squared	0.359	0.456
Adjusted R2	0.350	0.448

Note: ***Significance at $p < 0.01$

Impact of ESG on FP through the Moderating Role of MA

Testing of the second hypothesis involved the introduction of an interaction term of ESG*MA. Two regressions were run separately, one involving only the ESG (ESG*MA) whereas the other entailed three pillars of ESG (combined with MA) predicting the financial performance of firms. With the inclusion of the interaction term (ESG*MA), the stand-alone effect of the ESG on ROA remained positive ($\beta_1=0.008$) and significant (t-stat= 1.261) at $p < 0.05$. The combined effects of ESG and MA on ROA was also positive ($\beta_2= 0.028$) and significant (t-stat= 2.964) at $p < 0.01$, and enhanced beta value (from 0.008 to 0.028) portraying that the MA positively moderated the association between ESG and firm FP. For testing the effects of each pillar of ESG, the combined effects of ENV*MA and SOC*MA were positive and significant while GOV*MA was positive but insignificant, suggesting that GOV may not be a significant moderator to affect the relationship between ESG and FP. In case of Tobin’s Q, again two separate regressions were run as for ROA. It was found that standalone effect of ESG on Tobin’s Q remained positive and significant ($\beta_2= 0.258$ and $t = 1.845$ at $p < 0.1$). Introducing the interaction of MA

with ESG yielded a positive and significant coefficient ($\beta_2 = 0.659$ and $t = 3.195$ at $p < 0.01$), portraying that the MA positively moderated the association between ESG and firm FP and enhanced beta value (from 0.258 to 0.659). Similarly, for examining the effects of the three pillars of ESG when combined with MA, the combined effect of ENV*MA and SOC*MA on Tobin's Q were positive and significant, however in case of GOV*MA it was positive but insignificant (Table 4).

For control variables, it was found that firm size and GDP were negatively related to ROA, whereas age, cash, sales, and leverage were positively related. In the case of Tobin's Q, again firm size and GDP was negatively related, whereas leverage, age, cash and sales were positively related. The effects of control variables did not change enormously. Supporting literature for this finding indicated that managerial ability impacted all aspects of ESG implementation and its financial outcomes for the firms (Andreou et al., 2017; Berk & Rauch, 2016; Lins et al., 2016). A likely cause for the positive impact of superior managers on the financial performance of firms could be that investors perceived that firms with capable managers are more resilient and reliable in handling business challenges. The inference in reverse order can be that the firms with better financial performance are likely to have more capable managers (Cui, Jo, & Na, 2018; Lee et al., 2018).

Table 4

Results of Regression Analysis – Moderation by MA on ESG-FP Relation

	ROA	Tobin Q
ESG	0.008* (1.261)	0.258* (1.845)
ESG*MA	0.028*** (2.964)	0.659*** (3.195)
ENV	0.017*** (3.426)	0.526*** (4.732)
ENV*MA	0.023*** (2.973)	0.418** (2.508)
SOC	0.003 (0.641)	0.075 (0.661)
SOC*MA	0.019** (2.445)	0.528*** (3.124)
GOV	-0.007 (-1.242)	-0.059 (-0.469)
GOV*MA	0.012 (1.435)	0.246 (1.293)
Lev	0.051*** (6.722)	2.169*** (18.621)
Size	-0.005*** (6.203)	-0.338*** (22.731)
Sales	0.039*** (17.331)	0.642*** (21.541)
Cash	0.189*** (14.072)	1.615*** (14.047)
Age	0.004 (0.266)	0.005*** (2.839)
GDP	-0.013** (-2.235)	-0.009 (-1.312)
Industry Dummy	Yes	Yes
Year Dummy	Yes	Yes
Country Dummy	Yes	Yes
Constant	0.059*** (3.701)	6.055*** (12.044)
Observations	8,272	8,251
R-squared	0.361	0.387
Adjusted R2	0.348	0.498

***Significance at 0.01, **Significance at 0.05 levels, *Significance at 0.10.

Impact of ESG on FP through Moderating Role of Institutional Quality (IQ)

Test of hypothesis 3, entailed introduction of interaction terms of ESG*IQ and carrying out two sets of regressions one regression for only ESG and the other regression for the three pillars of ESG predicting firms’ financial performance. The analysis revealed that the effects of ESG on ROA continued to be positive ($\beta_1 = 0.015$) and significant ($t = 3.642$) at $p < .01$. For each pillar of ESG, the combined effects of ENV*IQ on ROA were positive ($\beta_2 = 0.010$) and significant ($t = 2.415$) at $p < .05$, SOC*IQ on ROA positive ($\beta_2 = 0.014$) and significant ($t = 4.121$) at $p < .05$, and GOV*IQ on ROA positive ($\beta_2 = 0.003$) but insignificant. The results indicated that the IQ did not moderate the association between GOV and firm FP. In case of Tobin’s Q, the interaction of IQ with ESG yielded a positive and significant coefficient ($\beta_2 = 0.195$ and $t = 2.259$) at $p < .05$, portraying that IQ positively moderated the association between ESG and firm FP. In case of independent pillars of ESG, the effects of ENV*IQ and SOC*IQ was positive and significant, whereas GOV*IQ on Tobin’s Q is negative and insignificant. The results supported sub-hypothesis but did not support for GOV when combined with IQ. Regarding control variables, the firm size and GDP were negatively related to FP (both ROA and Tobin’s Q), however for age, cash, leverage, and sales, they were positively related as presented Table 5.

Prior research generally corroborated the findings of this study. The rationale for the effective moderation of institutional quality on the financial benefits generated by ESG appeared multifaceted. Literature indicated that coercive pressure stemming from a regulatory standpoint is a consequence of the legal framework within a country (Barakat et al., 2015; Crawford & Williams, 2010). In the context of emerging economies, it appears that the institutional quality environment significantly influences the relationship between ESG and financial performance. ESG practices are relatively less esteemed in emerging economies, particularly where there exists a high prevalence of corruption, weak law enforcement mechanisms, ineffective regulatory oversight, and notably, issues of political and economic instability.

Table 5
Results of Regression Analysis – Moderation by IQ on ESG-FP Relation

Variable	ROA	Tobin Q
ESG	0.009* (1.917)	0.195** (2.259)
ESG_IQ	0.015*** (3.917)	0.502*** (6.367)
ENV	0.008** (2.018)	0.216*** (3.162)
ENV_IQ	0.010** (2.415)	0.242*** (3.863)
SOC	0.011*** (2.991)	0.122* (1.691)
SOC_IQ	0.014*** (4.121)	0.476*** (7.215)
GOV	0.014*** (4.121)	0.258*** (3.794)
GOV_IQ	0.003 (0.760)	-0.094 (-1.233)
Lev	0.034*** (8.648)	2.929*** (17.998)
Size	-0.003*** (6.127)	-0.322*** (25.256)
Sales	0.033*** (20.231)	0.653*** (22.458)
Cash	0.115*** (19.297)	1.605*** (13.926)
Age	0.006** (1.557)	0.005*** (2.183)
GDP	-0.002** (-2.113)	-0.006 (-1.208)
Industry Dummy	Yes	Yes
Year Dummy	Yes	Yes

Country Dummy	Yes	Yes
Constant	0.062*** (3.701)	6.012*** (14.096)
Observations	8,821	8,234
R-squared	0.342	0.464
Adjusted R2	0.353	0.451

Note: ***significance at $p < 0.01$, **significance at $p < 0.05$, *significance at $p < 0.10$

Impact of ESG on FP through Moderating Role of MA and IQ

The testing of fourth hypothesis was the culmination of this study which showed dual moderation of IQ and MA on the relation of ESG with FP. For this purpose, the double interaction term ESG*MA*IQ was introduced in the model. Like the previous analysis, two sets of regressions were run one for only ESG predicting the FP of firms and the other involving the three pillars as predictors of FP. It was found that the dual moderation effects of MA and IQ on the ESG-FP (both for ROA and Tobin’s Q) were positive and significant. In case of each pillar of ESG with ROA, the dual moderation effects of ENV*MA*IQ, SOC*MA*IQ and GOV*MA*IQ were positive and significant. However, in case of Tobin’s Q, the dual moderation effects of ENV*MA*IQ and SOC*MA*IQ were positive and significant whereas in case of GOV*MA*IQ, the result was negative and insignificant (Table 6). Past research works mostly focused on the significance and vitality of institutional quality in the improvement of financial performance (Farooq et al. 2013; Law & Habibullah, 2006; Saha & Ben Ali, 2017). However, only scanty work exists that has examined the association between institutional quality as well as managerial ability on the financial performance of firms in emerging economies.

Table 6

Dual Moderation Effects by IQ and MA on the Relationship between ESG and FP

	ROA	Tobin Q
ESG	0.008 (1.294)	0.250*** (3.114)
ESG_IQ	0.006 (0.671)	0.175* (1.738)
ESG_MA_IQ	0.016*** (2.825)	0.086*** (0.846)
ENV	0.001 (0.148)	0.099 (1.557)
ENV_IQ	0.005 (0.700)	0.337*** (3.951)
ENV_MA_IQ	0.008** (1.972)	0.139** (1.383)
SOC	0.014*** (2.725)	0.343*** (5.203)
SOC_IQ	0.002 (0.240)	0.040 (0.454)
SOC_MA_IQ	0.009** (2.134)	0.084** (0.826)
GOV	-0.001 (-0.195)	0.133* (1.882)
GOV_IQ	0.005 (0.626)	0.019 (0.201)
GOV_MA_IQ	0.010** (2.134)	-0.113 (-1.320)
Lev	0.046*** (-7.458)	2.369*** (19.132)
Size	-0.003***	-0.323***

	(5.112)	(24.954)
Sales	0.032***	0.598***
	(19.541)	(21.251)
Cash	0.124***	1.612***
	(20.311)	(14.112)
Age	0.000	0.002***
	(0.419)	(2.766)
GDP	-0.002**	-0.009
	(-2.113)	(-2.191)
Industry Dummy	Yes	Yes
Year Dummy	Yes	Yes
Country Dummy	Yes	Yes
Constant	0.109***	6.027***
	(3.143)	(13.198)
Observations	8,272	8,272
R-squared	0.391	0.461
Adjusted R2	0.342	0.398

Note: ***significance at $p < 0.01$, **significance at $p < 0.05$, *significance at $p < 0.10$

Discussion and Conclusions

This study, drawing from a dataset encompassing 750 international firms spanning the years 2010 to 2020, investigates the impact of ESG performance on firm financial performance (FP) within 13 Emerging Markets of Asia. The findings of this study reaffirm a positive and statistically significant relationship between ESG performance and firm FP, consistent with prior research findings (Chen, Song & Gao, 2023; Friede et al., 2015; Whelan et al., 2021). This underscores the notion that firms' FP tends to increase over time due to socially responsible investments in ESG practices and declines when engaging in irresponsible activities. Stakeholders such as investors, customers, employees, and regulatory bodies closely monitor the ESG behavior of organizations when making decisions. Firms demonstrating higher ESG performance tend to attract investors and customers, resulting in enhanced FP (Chen & Xie, 2022; El Khoury, Nasrallah & Alareeni, 2023). The individual components of ESG exhibited slightly varied strengths of relationships with financial performance (FP). Specifically, the environmental and social pillars of ESG demonstrated positive and significant associations with Return on Assets (ROA), while the governance pillar showed an insignificant (though positive) relationship. One plausible explanation for this divergence could be that firms in emerging economies might not fully adhere to governance protocols or provide comprehensive disclosures about governance practices (Chen & Xie, 2022). Firms with limited governance disclosure are observed to restrict their investment in ESG initiatives (Almeyda & Darmansya, 2019; Chen & Xie, 2022). However, all pillars showed positive and significant relationships with Tobin's Q, another measure of FP utilized in this study.

The positive impact of managerial ability (MA) on the relationship between ESG and financial performance (FP) has been consistently supported by various studies, indicating that ESG investments often stem from strategic decisions made by managers with higher MA, especially within contexts of managerial discretion (Gong, Yan, & Ho, 2020). These findings were robust, as the moderation by MA was significant for both measures of FP, namely Return on Assets (ROA) and Tobin's Q. The moderating role of MA on the relationship between ESG and FP was notably emphasized by Cho and Lee (2019), who argued that the influence of MA on ESG-FP relations is strengthened by managers with higher abilities, manifested through supportive ESG-related behaviors. The moderation effects of each pillar of ESG, as indicated by the coefficients of the interaction terms (MAENV, MASOC, and MA*GOV), were positive and significant for the environmental, social, and governance pillars concerning FP measured by ROA, albeit with varying levels of significance. However, for Tobin's Q, the moderation effect was insignificant only for the governance pillar.

Similarly, institutional quality (IQ) also played a significant moderating role in the relationship between ESG and financial performance (FP), consistent with findings from prior research (Karmani & Boussaada, 2021). High-

quality institutions characterized by well-defined business rules, reduced corruption, and effective enforcement of consistent policies tend to support ESG initiatives (Vatn, 2020). Consequently, firms adopt ESG practices to gain a competitive edge without resorting to unhealthy competition, shortcuts, or exploiting loopholes created by corruption. Both measures of FP (ROA and Tobin's Q) exhibited significant moderation effects of IQ on their relationship with ESG, indicating the robustness of the findings. Regarding each pillar of ESG, the moderation effects of IQ were positive and significant for the relationship between the environmental and social pillars and FP (both for ROA and Tobin's Q), albeit with varying levels of significance. However, the moderation effects of IQ on the relationship between the governance pillar and FP (both for ROA and Tobin's Q) were both negative and insignificant, suggesting a minimal role of IQ in governance aspects of ESG.

The dual moderation effects by both managerial ability (MA) and institutional quality (IQ) were positive and significant on the relationship between ESG and financial performance (FP), measured by both Return on Assets (ROA) and Tobin's Q. This dual moderation mechanism contributed to the enhancement of ESG practices and subsequently improved FP. While studies specifically analyzing the dual moderation by MA and IQ on the relationship between ESG and FP were scarce, indications of such effects could be inferred from the existing literature, indirectly supporting the findings of this study.

The behavior of firms is heavily influenced by the institutional environment, as preferences, values, and actions at all levels are shaped by institutional quality (Husted & Sousa-Filho, 2017; Vatn, 2020). Previous research suggests that firms often exhibit high levels of sustainable performance to gain legitimacy when faced with institutional pressures (Bansal, 2003; Bansal and Clelland, 2004; Berrone et al., 2010; Hoffman, 2001). Pressure from regulatory institutions compels organizations to appoint managers with superior MA, capable of meeting both institutional and stakeholder requirements for sustainability and legitimacy. In contrast, weak institutions characterized by corrupt practices and inconsistent policies fail to exert the necessary pressure on firms to change and align their behaviors with sustainable practices (Tuczek et al., 2018).

High-quality institutions, along with organizational leadership possessing higher managerial ability (MA), ensure that firms embracing ESG can achieve greater financial performance (FP) and meet stakeholders' expectations (Lacznik & Murphy, 1991). The Upper Echelon Theory and Institutional Theory suggest that managerial abilities translate into ESG-supportive actions when a conducive environment is present. These theories imply that stakeholders' expectations serve as motivators, while the firm's pursuit of legitimacy acts as a facilitator, encouraging enhanced ESG engagement (Nazari et al., 2015). Managers with greater MA are instrumental in assessing the beneficial returns on ESG investments and demonstrate a higher tolerance for uncertainty, aligning their actions with long-term corporate objectives. In emerging economies, institutional quality delineates the parameters for planning and implementing ESG activities by managers. Within these parameters, managers with higher MA visualize, plan, and execute ESG practices to advance the organizations' FP goals and integrate ESG into long-term organizational strategies.

The governance pillar of ESG demonstrated a weak association with firms' financial performance (FP) in both measures, namely Return on Assets (ROA) and Tobin's Q. Interestingly, despite moderation by institutional quality (IQ) and managerial ability (MA), both individually and jointly in the ESG-FP relationship, the link between the governance pillar of ESG remained weak and insignificant. This finding aligns with other studies and suggests a pressing need for firms to enhance their governance structures and adopt corporate governance protocols (Zubeltzu-Jaka et al., 2018). Transitioning to improved governance structures is likely to address issues related to legitimacy and trust within organizations to a significant extent (Kostova & Zaheer, 1999). To enhance governance, organizations should focus on bolstering the independence of governing bodies, fostering democratic decision-making processes, promoting gender diversity, and ensuring the independence of audit functions from executives (Gallego-Alvarez & Pucheta-Martinez, 2019). Additionally, mandating the disclosure of ESG performance for organizations can enhance transparency and accountability, further contributing to improved governance practices.

Practical and Theoretical Implications of the Study

Based on our findings, several policy and practical implications emerge. First, higher institutional quality fosters a conducive environment for business activities that benefit all stakeholders and society at large. This study

suggests that ESG practices, often discretionary in Emerging Markets, can be encouraged through institutional pressures. Therefore, the level of investment in ESG can be assessed by proficient managers who can effectively weigh the investment against considerations such as legitimacy, reputation, and financial outcomes.

Policymakers in government institutions play a crucial role in identifying inefficiencies, corrupt practices, and policy inconsistencies that undermine institutional quality, rendering them ineffective and unfriendly to businesses. Efforts should be directed towards addressing these issues to improve the overall business environment. Additionally, it is imperative to ensure that managers do not over-invest in ESG-related projects, especially in organizations with weaker financial statuses. Managers need to recognize the long-term benefits associated with ESG practices and carefully evaluate their potential impact on financial performance. Furthermore, managers should consider the institutional quality context in which firms operate to assess the availability of resources that can be allocated to ESG activities. By doing so, they can effectively enhance firms' financial performance while contributing to broader societal and environmental goals.

This study reinforces the positive and significant impact of ESG on firms' financial performance (FP), particularly within the context of emerging markets. While past research on emerging economies often focused on the impact of ESG on FP within a single country, region, or specific industry, this study utilizes a multi-country and multi-industry sample, leading to more generalizable findings. Against the backdrop of the institutional environment in Asian Emerging Markets, the study extends Institutional Theory and Upper Echelon Theory to include the role of managerial ability (MA) and institutional quality (IQ) in the relationship between ESG and firms' FP. Although FP can be enhanced through ESG adoption, managers with short-term perspectives may exhibit less inclination towards ESG practices. This situation is particularly concerning in Asian Emerging Markets, which already face ecological challenges exacerbated by factors such as global warming, population growth, pollution, and resource depletion, alongside a growing awareness of the importance of respecting employee and customer rights (Duque-Grisales & Aguilera-Caracuel, 2019).

Given the weaknesses observed in the governance pillar of ESG in Asian Emerging Markets, it is recommended that organizations adopt methodologies followed by Advanced Markets while adhering to globally accepted good governance practices to foster trust among all stakeholders. Moreover, in Asian Emerging Markets where official monitoring and regulatory mechanisms may be weak, proactive firm-level environmental and social initiatives should be encouraged and rewarded by institutions, with public acknowledgment for adhering to best practices. This approach can incentivize firms to prioritize ESG practices and contribute positively to both their own performance and broader societal well-being.

Limitations and Future Direction of Research

Certainly, there are several avenues for future research to address the limitations and further enhance our understanding of the relationship between ESG practices and firm financial performance:

Comparative Analysis: Conducting a comparative analysis between emerging and advanced markets could provide insights into the differences in ESG practices and their impact on financial performance. This approach could help identify areas where organizations in emerging markets may need to focus to improve ESG performance and financial outcomes.

Updated Data: Future studies should aim to use the most recent and updated data available beyond the year 2020 to capture the evolving landscape of ESG practices and their effects on firm financial performance.

Alternative Data Sources: Researchers should explore alternative sources or methodologies to gather data in cases where direct access to organizational data is limited, ensuring a more comprehensive analysis.

Double Moderation: Further investigation into the double moderating role of managerial ability (MA) and institutional quality (IQ) could provide deeper insights into their combined influence on the relationship between ESG and firm financial performance.

Multidimensional Approach: Adopting a multidimensional approach to analyzing firm performance, considering both financial and non-financial outcomes of ESG initiatives, could provide a more holistic understanding of the broader impacts of ESG practices on organizational sustainability and stakeholder value creation.

Non-linear Models: Exploring non-linear models that incorporate ESG, firm financial performance, IQ, and MA could uncover nuanced relationships and interactions among these variables. Techniques such as structural equation modeling or machine learning algorithms may be employed to capture complex relationships and potential threshold effects.

Addressing these limitations in future research endeavors can contribute to advancing knowledge in the field of ESG and its implications for firm performance, particularly in the dynamic context of emerging markets.

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