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EFFECTS OF FINANCIAL PERFORMANCE ON ESG PERFORMANCE: EVIDENCE FROM INDONESIAN SHARIA COMPANIES

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Abstract

The study correlates between Financial and ESG Performance in Indonesian Sharia-compliant companies, resulting in a significant research gap in Islamic finance. This study uses a panel data of 20 companies listed on the Jakarta Islamic Index (JII) from 2019 to 2023, totaling up to 100 company years. A multiple linear regression analysis is used to analyze the relationship between variables of ESG Score, Return on Equity, Total Asset, and Tobin's Q. The regression model indicates a significantly positive correlation with ESG performance. Specifically a 1 percentage point increase in ROE is associated with a 0.245 increase in ESG score, showing a model where financial performance facilitates sustainability. Company size and market valuation do not exhibit significance towards ESG performance. Findings recommend companies with robust ROE suggesting good financial health and ESG leadership potential with Sharia-compliant firms. This study presents empirical evidence comparing financial and ESG performance within the Indonesian Islamic capital market. It challenges conventional paradigms of "sustainability performance driving financial" and instead suggests the other way around. This study provides significant insight into an expanding global Islamic finance sector while advocating for integrated Islamic ESG frameworks that acknowledge financial performance as a basis for effective sustainability implementation

Keywords: Financial Performance, ESG Performance, Jakarta Islamic Index, Tobin's Q

INTRODUCTION

The relationship between Environmental, Social, and Governance (ESG) factors and financial performance has become a critical area of inquiry in contemporary finance. While empirical evidence demonstrates predominantly positive associations between ESG practices and financial outcomes in developed markets, significant contextual variations exist, with some studies showing negative relationships, particularly in Indonesia and Vietnam. This complex and context-dependent nature of ESG's financial implications necessitates region-specific analysis to understand the true dynamics within different economic and cultural frameworks (Rumansyah & Nainggolan, 2025). No longer focusing on merely a single dimensional objective of profit, but now has shifted more and more towards a Triple Bottom Line approach, or also known as 3P (People, Planet, Profit) (Le Bruyn Goldeng & Burki, 2021). This shift of mindset has been caused by a lot of factors, with massive cases such as the BP Oil Spill as one of the major examples that prompted this shift of paradigm. Empirical research reveals substantial industry-specific variations in ESG-financial performance relationships. European banks experience increased operational costs due to environmental governance, while green energy investments positively influence return on investment (ROI) in the energy sector. The manufacturing sector demonstrates more consistent positive ESG effects, with companies better positioned to align financial

performance with sustainability initiatives through higher revenue growth enabling better ESG integration. Recent analysis of ASEAN-5 banking companies (2019-2023) reveals that environmental and social pillars do not significantly impact ROE, while the governance pillar demonstrates significant positive relationships with financial performance, highlighting the critical role of corporate governance in the financial services sector (Destyana & Mareta, 2025; Hakim et al., 2025; Rizki & Putra, 2024).

As a growing and developing nation, Indonesia has a significant presence in the global stage as a relatively young country having their forests and protected territories as a huge foundation. Starting from Indonesia's presidency on the global stage of G20 (PwC, 2023), spearheading ESG-related goals to have the backing and support of the top 20 countries in the world. Also as one of the founding fathers of the Non-Aligned Movement (Putra & Satria, 2025), Indonesia also has the trust of developing countries all over the world. With a steadily growing population towards Indonesia's Golden Age at 2045 and the ever-increasing economy competing with fellow neighbors, Indonesia is projected to increase its ESG investment by around 50%, increasing to 45 billion US Dollars by 2030 with of course industries such as energy & renewable energy and green buildings taking the spotlight in the next coming years (JCSS, 2025). Not to mention a different viewpoint or perspective towards ESG, Indonesia also has the largest Islamic population in the world. Considering how differently are things run under a secularism viewpoint, this point becomes a point of interest especially in corporate governance.

Indonesia's Islamic capital market has demonstrated exceptional growth, with the Indonesian Stock Exchange recognized as one of the best Shariah capital markets globally for four consecutive years. The Indonesian Shariah Stock Index (ISSI) grew by 6.02% in 2022, while ISSI's market capitalization increased by 6.92% to IDR 4,259.24 trillion. Indonesia's position extends beyond market size to strategic leadership in sustainable Islamic finance development, with comprehensive roadmaps integrating Islamic banking, capital markets, and non-bank financial institutions (Haryadi, 2017; Maulida et al., 2023; Waqqosh et al., 2023).

The research significance extends to critical policy implications for Indonesia's developing Islamic capital market. Islamic Financial Institutions lag behind conventional banks in ESG disclosure due to lack of structured frameworks aligned with Shariah principles, creating urgent need for empirical evidence to inform regulatory frameworks and industry standards. As sustainable sukuk issuance is expected to reach \$10.0-12.0 billion in 2025, robust empirical understanding of ESG-financial performance dynamics becomes essential (Damak et al., 2025; Sori et al., 2025).

The global Islamic finance industry has experienced extraordinary expansion, with assets reaching USD 5.4 trillion in 2024 and forecasted to grow to USD 9.75 trillion by 2029, representing a CAGR of 10%. This remarkable growth reflects increasing recognition of Islamic finance's inherent alignment with ESG principles and sustainable development objectives. Islamic banking comprises around 70% of total assets, while sukuk and Islamic funds increasingly contribute to sector growth. Southeast Asia, led by Malaysia and Indonesia, represents approximately 20% of total assets with projections to reach \$3 trillion by 2029 (Rai, 2024). This remarkable expansion reflects not merely market demand but also the increasing recognition of Islamic finance's inherent alignment with ESG principles and sustainable development objectives (Coalition Greenwich, 2025; Rai, 2024). Islamic banking remains the

dominant segment, comprising around 70% of total assets, while sukuk and Islamic funds are increasingly contributing to sector growth. The integration of sustainability principles has emerged as a key trend, aligning Islamic finance with the global sustainable finance movement. Southeast Asia, led by Malaysia and Indonesia, constitutes the second-largest market, representing approximately 20% of total assets, with assets projected to reach \$3 trillion by 2029 (Coalition Greenwich, 2025).

The theoretical foundation for ESG integration within Islamic finance rests on the natural convergence between Shariah principles and ESG objectives. This alignment manifests through several key dimensions (Al-Taitoon et al., 2023; Judijanto et al., 2025). Environmental Stewardship (Khalifah Concept): Islamic finance emphasizes environmental responsibility through the concept of Khalifah (stewardship), which mandates sustainable resource management and prohibition of excessive waste (Israf). This theological foundation aligns naturally with environmental sustainability goals and supports long-term value creation perspectives. (Al-Taitoon et al., 2023; Judijanto et al., 2025). Social Justice and Welfare (Maqasid Shariah): The Maqasid Shariah framework prioritizes societal welfare (Maslaha) over pure profit maximization, creating inherent alignment with social responsibility dimensions of ESG. Islamic finance's prohibition of harmful industries (gambling, alcohol, tobacco) reflects embedded social responsibility concerns, while the stakeholder-oriented approach considers community interests alongside shareholder value. (Anisa, 2025; Ihsan et al., 2021; Irsyad et al., 2025; Lubis, 2023; Milena & Stefan, 2025). Governance Excellence and Transparency: Shariah governance requirements mandate enhanced transparency and disclosure standards, creating natural alignment with governance dimensions of ESG. The presence of Shariah Supervisory Boards (SSB) and compliance with AAOIFI standards contribute to stronger governance frameworks, while ethical business conduct is fundamental to Islamic commercial principles. (Al-Taitoon et al., 2023; Ihsan et al., 2021; Lubis, 2023; Milena & Stefan, 2025).

Despite the natural theoretical convergence between Islamic finance and ESG principles, empirical research examining the specific relationship between financial performance and ESG scores in Islamic contexts remains limited. Recent studies reveal significant variability in ESG disclosure among Islamic Financial Institutions, with governance disclosures at 22.3%, social disclosures at 13%, and environmental disclosures at only 2.4%. This disclosure gap creates urgency for systematic empirical analysis (Judijanto et al., 2025; Milena & Stefan, 2025; Sori et al., 2025). Existing research demonstrates mixed findings specific to Islamic contexts. While some studies indicate Shariah-compliant firms with strong ESG factors exhibit superior stock performance, others show energy sector Shariah companies having lower sustainability performance than conventional companies. These contradictory findings necessitate comprehensive empirical investigation to clarify relationship dynamics within authentic Islamic finance frameworks (Awaludin et al., 2025a; Modjo et al., 2025).

This research addresses the critical need for context-specific ESG analysis that recognizes the distinctive characteristics of Islamic finance principles and their natural alignment with sustainable development objectives. Unlike previous studies focusing on single ESG dimensions or limited financial indicators, this research provides holistic analysis of multiple financial performance measures (Market Capitalization, ROE, ROA, Total Assets, Tobin's Q) in relation to comprehensive ESG scores within the

unique context of Shariah-compliant companies. As the global Islamic finance industry approaches USD 7.5 trillion by 2028, empirical evidence from Indonesia's leading Islamic capital market provides invaluable insights for international Islamic finance development and global sustainable finance integration. This research contributes to bridging the gap between Islamic finance theory and sustainable finance practices, offering essential empirical foundations for advancing integrated frameworks of Islamic finance and sustainable development across the rapidly growing global Islamic finance ecosystem (Neo & Khadra, 2025).

This paper aims to contribute into the relationship between financial performance and sustainability performance. According to Whelan et al. (2021), there are still numerous contradicting results, where 58% of results from research conducted in 2015-2020 proved a positively significant relationships between ESG or sustainability performance and financial performance. Meanwhile, 8% showed negative results, with 13% showing neutral impact, and another 21% providing mixed results. Whilst the majority of research suggests a positive impact between the two performances indicators, this paper studies into the proof of these research in the context of Islamic or Sharia-compliant firms in Indonesia. The reasoning behind this considers the recent implementation of the Financial Services Authority recently ratifying the obligation of publicly listed companies to publish or arrange a sustainability report for the stakeholders. Despite already being able to see the impact between the two performance indicators, this research aims to verify whether that phenomenon is also occurring in the Islamic market to show progress of sustainability performance being a reality. This perspective is taken considering the world's current priority in realizing the UN's SDGs to make the world a better place.

Various studies relate Return on Equity (ROE), Total Assets (TOA), and Tobin's Q (TBN) to the Refinitiv ESG Score for sustainability or ESG performance, including those grounded in stakeholder theory (Awa et al., 2024; Freeman et al., 2025; Mahajan et al., 2023; Talan et al., 2024), agency theory (Al-Faryan, 2024; Del Gesso & Lodhi, 2025; Fleckinger et al., 2024; Kismawadi, 2025), and Islamic finance theoretical frameworks (Risman, 2024; Shalhoob, 2025; Yasmeen et al., 2024), specifically integrating Maqasid Shariah principles with contemporary ESG considerations (Agustin et al., 2023a; Mohd Zain et al., 2024).

The relationship between Return on Equity and ESG performance in Islamic finance contexts is anchored in stakeholder theory (Awa et al., 2024; Freeman et al., 2025; Mahajan et al., 2023; Talan et al., 2024), resource based theory (Chatterjee et al., 2024; El Nemar et al., 2025; Kumar & Gembali, 2025; Razzaque et al., 2024) and the Khalifah (stewardship) concept fundamental to Islamic business principles (Khan et al., 2024; Naseeb, 2024; Rahmat et al., 2025). ROE (El Abiad et al., 2024; Tutcu et al., 2024), as a measure of operational efficiency, represents a company's ability to generate value from its resources and invest in comprehensive ESG initiatives, which aligns with Islamic concepts of utilizing shareholders' funds in accordance to Sharia principles, creating capacity for broader stakeholder value creation through ESG activities (Agustin et al., 2023b; Akbar & Setiana, 2024; Alghafes et al., 2024a; Awaludin et al., 2025b). Recent empirical evidence demonstrates mixed but predominantly positive relationships between ROE and ESG in Islamic contexts. Malaysian Islamic finance studies show ESG coefficients of 0.126 for ROE (El Abiad et al., 2024; Fahrullah et al., 2024; Tutcu et al., 2024), indicating positive associations. GCC Islamic banks

analysis revealed that social components positively affect ROE, while governance impacts Return on Equity specifically (Alghafes et al., 2024b; Suprapto et al., 2025).

The relationship between firm size (measured by total assets) and ESG performance is theoretically grounded in resource-based theory (Chatterjee et al., 2024; El Nemar et al., 2025; Kumar & Gembali, 2025; Razzaque et al., 2024) and institutional theory (Galleli & Amaral, 2025; Li & Bosma, 2025; Schiavi et al., 2024). Larger firms typically possess greater financial resources, enhanced capabilities, and stronger institutional pressures to engage in ESG activities. Within Islamic finance contexts, firm size may influence ESG performance through enhanced capacity for Sharia governance implementation and greater stakeholder expectations (Milena & Stefan, 2025). Extensive empirical evidence supports positive firm size-ESG relationships across multiple contexts. Studies demonstrate that larger firms exhibit superior ESG disclosure and performance due to increased stakeholder scrutiny, regulatory pressures, and resource availability. Asian market research indicates that firm size significantly moderates ESG-performance relationships, with larger companies showing stronger ESG effects on firm value (Elrayah & Mirzaliev, 2024; Yuliyanti et al., 2025).

The relationship between Tobin's Q (market valuation) and ESG performance is theoretically supported by signaling theory (Connelly et al., 2025; Hussain et al., 2024; Lu et al., 2024) and agency theory (Al-Faryan, 2024; Del Gesso & Lodhi, 2025; Fleckinger et al., 2024; Kismawadi, 2025). Tobin's Q (Lee et al., 2024; Lim & Mali, 2024; Tho, 2024), representing market perceptions of firm value relative to asset replacement costs, captures investor expectations regarding long-term value creation and risk management effectiveness. Within Islamic finance contexts, market valuation reflects investor confidence in Sharia-compliance quality and sustainable business practices alignment with Islamic principles (Modjo et al., 2025; Sori et al., 2025). International research demonstrates predominantly positive relationships between Tobin's Q and ESG performance, with higher ESG scores associated with premium market valuations. Asian market studies confirm that ESG disclosure positively influences Tobin's Q, reflecting market recognition of sustainability efforts. However, crisis period analysis reveals mixed results, with some studies showing negative ESG effects on market valuation during economic uncertainty (Rao & Juma, 2024; Solikhah & Weng, 2024; Zulianto & Aisjah, 2025).

With the growth of importance and significance in ESG, companies are expected to prioritize their strategic directions and integrate ESG into their decision making. There is a need to study the performance related to ESG not just in the conventional business world, but also in the world of Islamic finance to then compare whether it is in the leading position or behind the average performance. Considering the significance of Islamic finance, especially here in Indonesia, it is a growing giant that needs to be tended to. With that, this research aims to answer a few research questions proposed by this research. This research wishes to examine whether there is a significance from financial performance towards sustainability performance in the context of Sharia-abiding companies, in this context being the JII listed companies. There are 3 variable indicators for financial performance, them being Return on Equity, Total Asset, and Tobin's Q, and one for sustainability performance, being ESG Score from Refinitiv. This research questions the relationship between those variables.

Through quantitative methods of multiple linear regression analysis, this

research examines the relationship between financial performance and sustainability performance utilizing a panel data of 20 companies and each having 5 years. By examining the relationship, this research would examine the existence of Sharia principles such as *Khalifah* and *Maqasid-Sharia* to verify whether the difference of those principles in Sharia-abiding companies do have an effect and also bring another level of concern and focus for companies, providing a better and more holistic approach in certain matters. Examining these variables in a different context would determine whether the difference in these factors are actually a significant change in companies. A further examination would be required to identify these different factors, but this type of research would provide an observation and dive into the topic of financial and sustainability performance in an Islamic context. At the end of this research, it is expected that said research will become a base for future research of diving into the topic more and identifying more factors to further push sustainability performance as a focus or initiative towards the Sustainable Development Goals made by the United Nations.

METHODOLOGY

Research Type

This research uses a quantitative approach in analyzing the relationship between variables. As mentioned previously, there will be 3 variables of financial performance being independent variables and another variable of sustainability performance. The 3 variable indicators of financial performance are Return on Equity (ROE), Total Assets (TOA) and Tobin's Q (TBN). Meanwhile the sustainability performance will have an indicator of ESG Score (ESG).

Population and Sample

This research uses JII (Jakarta Islamic Index) listed companies as the sample in this research. Out of the 30 companies listed in the Index, only 20 companies are chosen due to the lack of data, as some of the companies have only been listed recently or even after our choice of time selection. Using a panel data, each company has 5 years worth of data, comprising up to 100 company-years of observations. Table 1 shows the descriptive statistics of all 100 company-years with a variation of results.

Data Collection Method

This research uses secondary data collected from the Refinitiv database. Firstly Indonesian companies are filtered out and gathered their data based on the IDX Index. Secondly, JII listed companies are identified and taken out of the list. Said data are used before checking again the completeness of the data which is then filled in by manually inputting from their respective financial reports.

Definitions and Operationalization of Variables

Prior to conducting the analysis, Table 1 presents the conceptual and operational definitions for each variable, ensuring clarity regarding their measurement and interpretation

Table 1
List of Variables

Variable	Abbreviation	Description	Nominal Range / Formula
ESG Score	ESG	Score of company ESG Performance based on Refinitiv	0-100
Return on Equity	ROE	Measuring the company's profitability relative to its total equity	Net Income / Shareholder's Equity
Total Assets	TOA	Total of asset owned by the company at the end of the fiscal year	Current Assets + Fixed Assets
Tobin's Q	TBN	Compares company's market value towards its book value	Market Capitalization / Total Assets

Source: Fieldwork Research, Data processed by author (2025)

Analysis Technique

This research utilizes correlation analysis and multiple linear regression analysis to first check the correlation between variables, then the significance of each hypothesis. As each and every variables used in this study is of different measures and scales, a normalization method of natural logarithms will be implemented for the variables of Tobin's Q and Total Assets to match their scales closer to ESG Score and Return on Equity.

RESULT AND DISCUSSIONS

Research Result

Descriptive statistics were calculated to summarize the central tendency and dispersion of the study variables. The results are presented in Table 2.

Table 2

Descriptive Statistics

Variable	Obs	Mean	Std. dev.	Min	Max
ESG	100	54.29169	17.7779	13.76139	87.52229
ROE	100	19.73315	26.58366	-11.046	130.129
TOA	100	8.196453	7.763883	-3.552	36.81
TBN	100	1.635063	2.473052	.2517432	15.51912

Source: Fieldwork Research, Data processed by author (2025)

Judging from the standard deviation, the variability of Tobin's Q show a tighter spread compared to other variables, especially ROE with the highest variability of all the other variables. Looking at the minimal value of ESG score of 13.76, there is a possibility of companies not disclosing enough information to guarantee a high score on the ESG performance. Taking the ESG Score from the Refinitiv database, the evaluation of ESG performance is based on publicly available information, especially considering the recently implemented sustainability-related regulations in Indonesia with the Circular Letter number 51 year 2017 regarding Implementation of Sustainable Finance requiring the must for sustainability reporting.

To assess the strength and direction of the linear association between the variables, the correlation matrix is presented in Table 3.

Table 3

Correlation Analysis

Variable	ESG	ROE	TOA	TBN
ESG	1.0000			
ROE	0.1861	1.0000		
TOA	0.0221	0.2950	1.0000	
TBN	-0.0064	0.3961	0.3380	1.0000

Source: Fieldwork Research, Data processed by author (2025)

Comparing the correlation between variables, the highest correlation is between ROE and TOA with Tobin's Q. Considering the formula of Tobin's Q, it takes into account the market value of assets, which is directly correlated to TOA for Total Assets, and the replacement cost of capital which is correlated to ROE for the Equity component. Despite that, there is not too strong of a correlation between ESG and the other variables, but this may also be due to the small volume of ESG score in the data used.

The results of the regression analysis conducted to test the hypotheses are presented in Table 4

Table 4

Multiple Linear Regression Analysis

		Variables	Estimate	S.E.	C.R.	P
H1	<---	ROE – ESG	.2454535	.0791459	3.1	0.003
H2	<---	TOA – ESG	.5949757	2.123088	0.28	0.780
H3	<---	TBN - ESG	-2.876389	2.442064	-1.18	0.242
		constant	36.10419	47.42988	0.76	0.448

Source: Fieldwork Research, Data processed by author (2025)

The multiple linear regression analysis indicates that the model examining the relationship between ESG scores and predictive parameters such as Return on Equity (ROE), total assets (TOA), and Tobin's Q (TBN) is statistically significant, as evidenced by the F-test ($p = 0.0204$). The model, however, explains for just a small fraction of the variation in ESG ratings ($R^2 = 9.65\%$). The sole factor exerting a significant and favorable impact on ESG ratings is ROE, with a coefficient of 0.2455 ($p = 0.003$). This indicates that a higher ROE correlates with an elevated ESG score. The logarithm of total assets and the logarithm of Tobin's Q, conversely, are ineffective predictors since their p-values indicate a lack of statistical support for their association with ESG ratings. The confidence interval for ROE excludes 0, indicating its significance. Conversely, the confidence intervals for the remaining predictors encompass zero, indicating their lack of significance. In general, the model is beneficial; nonetheless, it is ineffective in generating accurate forecasts. In this instance, ROE is the one unequivocal indicator of ESG performance.

Discussions

Indonesia has only recently come into the sustainability reporting game. The Circular Letter from the Financial Services Authorities (OJK) number 51 year 2017 has only recently put Indonesia in the map of Sustainability Reporting. This Circular Letter requires all publicly listed companies to publish and disclose information regarding sustainability. Furthermore, the Circular Letter number 16 year 2021 further details the components required to be disclosed in the sustainability reporting. The amount of data and experience pales in comparison to other countries such as North America at 97% (KPMG, 2022). G250 and N100 companies report sustainability information at a rate of 96% and 79% respectively, showing a massive increase in the need of sustainability information, especially with the extreme rise in the mid 2000's. Countries such as the USA, Germany, Japan, and Singapore all have 100% rate of sustainability reporting rates. Those countries are then followed by the UK, South Korea and Malaysia at a rate of 99%. This shows the ever-growing need of the sustainability reporting.

While the overall F-test confirms the statistical significance of the model, the low R-squared value of 9.65% necessitates a stronger acknowledgment of the model's limitations. This value indicates that while ROE is a robust predictor, the current model—relying only on these three financial indicators—only explains a very small fraction of the total variation in ESG scores. The limited explanatory power highlights that non-financial factors, such as the company's industry-specific risks, the maturity of its ESG disclosure practices, or broader regulatory environments, likely play a substantially larger role in determining the Refinitiv ESG Score for JII-listed companies. Consequently, the model should be viewed primarily as a demonstration of a significant prerequisite (profitability enables sustainability), rather than an effective tool for accurate forecasting of ESG performance

Throughout the years, the Islamic financial markets have been rising and also following trends towards sustainability. A few papers have also shown the positive effect of financial performance with sustainability performance from the ROE perspective (Suprapto et al., 2025). Malaysian Islamic companies also show similar results of the financial performance (Fahrullah et al., 2024). Considering Sharia laws, Khalifah or Environmental Stewardship requires companies to be able to responsible to environmental situations, hence aligning said companies to environmental protectionism. This principle motivates and pushes Islamic or Sharia-abiding companies to be able to reinvest the profit towards environmental initiatives. Maqasid Shariah or social justice also shows the higher ROE towards ESG performance with a focus and priority on Social Welfare contributions, reflecting a fundamental stakeholder-oriented approach. On top of that, Sharia Supervisory Boards creates enhanced transparency standard to maintain and ensure that better quality on corporate governance.

Conversely, the analysis indicates that both Total Assets (TOA) and Tobin's Q (TBN) are statistically insignificant in predicting ESG performance. This finding challenges conventional finance literature, where firm size and market valuation often show a strong correlation with ESG commitment due to greater public scrutiny and resource availability. We posit that this lack of significance in the Indonesian JII context stems from the mixed-industry nature of the index. The JII includes companies from highly disparate sectors (e.g., manufacturing, infrastructure, finance), which are at

different stages of ESG maturity and face varying regulatory pressures for disclosure. Consequently, a large size (high TOA) in one sector might not translate to the same ESG capacity or investor pressure as a large firm in another sector. Furthermore, the volatility and liquidity dynamics of the Indonesian market may dilute the predictive power of Tobin's Q, suggesting that the current market valuation does not yet fully capitalize on a company's non-financial ESG performance, a condition that may improve as the Sharia capital market matures.

Despite all that, there is a variation between the companies in the sample used as each and every company listed in JII has different industries and sectors, where the correlation or effect may not be translated well to market recognition (Chen & Zhang, 2024; Naeem et al., 2022). Taking into note other possible factors, the relationships between variables relatively insignificant in this context due to reasons of data volume, similarities between companies and lack of syaria-abiding specific performance indicators that may show more clearly the presence of Islamic-style management into the statistical analysis.

The findings in this paper suggest that profitable Islamic companies are more able to enhance ESG performance with a "financial performance enables sustainability performance" approach model, rather than using sustainability to drive financial performance. This has been a very commonly misunderstood concept of the association between financial performance and sustainability performance. This misunderstanding leads on to activities such as greenwashing, which uses "green" concept to show the products being green and sustainable rather than actually implementing sustainability in the supply chain. This paper also recommends that investors should prioritize companies with strong ROE performance as indicators of both financial health and potential ESG leadership among Sharia-compliant companies. The integration of ESG and Sustainability in business strategies and reporting standards also support Islamic firms in committing to both Khalifah and Maqasid Shariah hence increasing the potential in these fields. Meanwhile seeing the insignificance of Total Assets towards Tobin's Q, this suggests that whatever the size of the firm, it does not hinder or distract the company's focus on conduction stewardship on ESG, which explains a different approach of Sharia-compliant companies to the current issue of ESG. Meanwhile for Tobin's Q, considering its components of equity and asset accounts, different rates of Tobin's Q also do not affect the performance of ESG activities or initiatives. This part suggests that there is no focus on building up equity while executing green projects or sustainable initiatives. An approach of greenwashing to look green just to garner investor support is not prominent in the context of JII, hence shows a lot more sense of responsibility among the management.

Putting a spotlight on the relationships started by Tobin's Q and Total Asset, this massively brings a contradiction into discussion. Resource-Based Theory (Chatterjee et al., 2024; El Nemar et al., 2025; Kumar & Gembali, 2025; Razzaque et al., 2024) suggests that with the provision of asset and resources, companies are able to conduct strategic initiatives especially in the condition where resources are in excess. The insignificance of Total Asset towards ESG shows the contradiction and point out another picture where even despite the lack of resources, companies are still able to conduct sustainability-related initiatives and activities. This is related to the concept of Khalifah (stewardship) where companies are, nonetheless, entrusted to

take care of the environment around and ensure equilibrium. Whereas Tobin's Q show a contradictory relationship as opposed to the signalling theory (Connelly et al., 2025; Lu et al., 2024). Considering the equation, Tobin's Q has components of the company's asset and the shareholder's equity, linking the two components together. Equity describes the presence of shareholders acting as the principal, expecting the company, acting as the agent, to conduct operations and initiatives well. A negative relationship between Tobin's Q and sustainability performance shows that the shareholders might not have that much of a priority when it comes to sustainability initiatives and activities. Despite that, other cases and contexts may be possible, such as share price being irrelevant or the market condition might not necessarily be relevant to sustainability related matters.

CONCLUSION

This research provides empirical evidence on the relationship between financial performance and ESG performance within Indonesian Shariah-compliant companies listed on the Jakarta Islamic Index (JII) from 2019-2023. The findings contribute significantly to the growing body of literature examining the intersection of Islamic finance principles and sustainable development practices. The regression analysis of 100 company-year observations from 20 JII-listed companies reveals critical insights into the ESG-financial performance nexus within Islamic contexts, where ROE demonstrates a statistically significant positive relationship with ESG performance remaining robust with a 95% confidence interval excluding 0. Due to the variation of industries, company size measured by total assets and market valuation measured by Tobin's Q does not show significant relationship with ESG performance.

Theoretically and for academics, this paper contributes by supporting the “financial performance drives sustainability”, hence challenging traditional assumptions regarding the correlation between ESG and financial performance causality, especially in the Islamic context. This paper helps validate the theoretical convergence between Shariah principles and ESG objectives, demonstrating profitable Islamic or Sharia-abiding companies are better positioned to implement sustainability initiatives. It also draws a landscape especially for the gap not yet covered for Sharia-abiding companies in Indonesia. Whereas for investors, the paper recommends prioritizing companies with strong ROE performance as it translates into ESG performance eventually due to it being a foundation for healthy funding for sustainability performance. Corporate management may use this paper to integrate sustainable profitability in business planning as a prerequisite for comprehensive ESG implementation. Policy makers should also take note of integrating Islamic standards with ESG frameworks that might also be a one-stop solution for Islamic-ESG reporting, especially considering the massive increase in the Islamic Finance Industry that might reach up to USD 7.5 trillion by 2028.

Research limitations include the availability of data, considering the very small amount of Sharia-abiding companies listed in the JII index on top of the small amount of ESG Score performance for said companies. Due to this fact explicitly, it mirrors on the R-squared of the value which show a relatively weaker description of the relationship between variables. This may also point out the scarcity of data regarding ESG Performance due to the companies of Indonesia only coming into the

race quite recently. Other than that, other financial performance indicators are needed to maybe show a higher rate of significance between data. Other than that, the JII index includes companies from all industries, hence the results are not well translated into the results.

In the future, researchers are recommended to use a longer time series data with more companies in the sample to show more statistical power and generalizability. Other than that, researchers may also use the ISSI (Indonesian Shariah Stock Index) with 400+ companies rather than just JII with 30 companies in the index that may be able to increase the R-squared value and increase as well the significance of this model. Research models such GMM estimation and structural equation modeling (SEM) may also provide a better analysis towards the given data. Whereas regarding the variables itself, future research may include more Islamic-specific indicators such as Shariah Supervisory Board quality, Islamic social responsibility metrics, and compliance with Maqasid Shariah principles to better reflect the implications of Islamic or Sharia-compliant companies towards the ESG performance measured. To build a better comparison and capture a larger general characteristics, conducting cross-country analysis would be better to examine cultural and regulatory differences. With this, researchers may also be able to develop an Islamic ESG benchmarking framework to further improve the already significant market of Islamic capital market.

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