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Bridging Profitability and Sustainability: Insights from Carbon Emission Disclosures and Governance Practices

Muryani Arsal[1]*, Wildani[1], Ismail Badollahi[1]

[1]Universitas Muhammadiyah Makassar, Indonesia

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***Corresponding author:** Muryani Arsal
Universitas Muhammadiyah Makassar, Indonesia

Abstract

Background: This study investigates the impact of Good Corporate Governance (GCG), profitability, and carbon emission disclosure on firm value in the mining sector listed on the Indonesia Stock Exchange (IDX) from 2019 to 2022. The mining sector's significance in Indonesia's economy and the growing importance of sustainable corporate practices provide the context for this research. Methods: The study employs multiple regression analysis to analyze data from 11 mining companies. The variables include GCG mechanisms (managerial ownership, institutional ownership, independent commissioners, and audit committees), profitability (measured by Return on Assets), and carbon emission disclosure. Firm value is proxied by Tobin's Q. Results: The findings indicate that profitability has a positive and significant impact on firm value. However, GCG mechanisms such as independent commissioners and audit committees have negative effects on firm value. Carbon emission disclosure does not significantly influence firm value. Conclusion: The study highlights the importance of profitability in driving firm value but also underscores the need for effective GCG mechanisms and greater emphasis on environmental responsibility. The results contribute to the discourse on sustainable corporate practices and their implications for investor confidence, emphasizing the necessity of balanced approaches that integrate financial performance with environmental sustainability.

Keywords: Good Corporate Governance, Profitability, Carbon Emission Disclosure, Firm Value, Tobin's Q, Mining Sector.

INTRODUCTION

The mining sector plays a pivotal role in the economic growth of countries globally. According to the World Bank, 56 nations are classified as mining economies, directly involving over 3.9 billion individuals in mining-related activities. In these countries, mining contributes significantly to gross exports, often exceeding 50% of total export value in at least 20 nations. Indonesia's mining sector—spanning coal, oil, and gas—contributes significantly to national economic development. In 2022, the mining sector contributed substantially to Indonesia's GDP, which reached IDR 19 quadrillion, marking a critical area of focus for both domestic and foreign investors.

Market dynamics in the mining sector are characterized by fluctuating stock prices, making it a vital area for investors seeking to maximize returns. Mining companies saw their stock indices rise by 16.61% in 2018 despite an overall market downturn, signifying investor confidence amidst sector-specific opportunities. However, the long-term viability of mining enterprises increasingly hinges on how they balance profitability with environmental sustainability and governance.

Environmental concerns have come to the forefront of corporate performance assessments (Arsal & Hasanuddin, 2019). Climate change, exacerbated by industrial activities, has prompted global efforts to curb greenhouse gas emissions. With Indonesia ranking as the sixth-largest contributor to global carbon dioxide emissions, the country faces mounting pressure to align its mining practices with international sustainability standards. Consequently, carbon emission disclosure has emerged as a critical indicator for evaluating corporate accountability and environmental performance (Kurnia *et al*., 2021).

Governance structures such as Good Corporate Governance (GCG) have been recognized as mechanisms to mitigate agency conflicts and enhance corporate value. By integrating transparency,

accountability, responsibility, independence, and fairness (Poletti-Hughes & Briano-Turrent, 2019; Schillemans & Bjurstrøm, 2020). GCG mechanisms like managerial and institutional ownership, independent commissioners, and audit committees help align management decisions with stakeholder interests (Boubaker *et al*., 2016; Vitolla *et al*., 2020). Profitability, another critical determinant of firm value, provides insights into a company's operational efficiency and its potential to deliver returns to investors (Arsal, 2021; Arsal, Dewisari, *et al*., 2024). Together with carbon emission disclosures, these factors offer a comprehensive framework for evaluating the multifaceted drivers of corporate value (Pipin *et al*., 2020).

This study aims to explore the relationships between GCG, profitability, and carbon emission disclosure, and their collective impact on firm value. Using Tobin's Q as the proxy for firm value, the study provides empirical insights into how these dimensions interplay within the context of Indonesia's mining sector. By bridging theoretical constructs with real-world data, this research contributes to the discourse on sustainable corporate practices and their implications for investor confidence.

Agency Theory and Governance Mechanisms

Agency theory explores the conflicts of interest that arise in principal-agent relationships. In a corporate context, these relationships are most evident between shareholders (principals) and company executives (agents) (Mahrani & Soewarno, 2018; Tjahjadi *et al*., 2021). Shareholders seek to maximize firm value, while managers may prioritize their personal interests, leading to agency costs. Governance mechanisms serve to align these divergent interests by establishing systems of control and accountability (Riyadh *et al*., 2023).

One of the foundational mechanisms of governance is managerial ownership. When managers hold significant shares in the company, they are incentivized to act in the best interests of shareholders because their personal wealth is tied to firm performance (Aggarwal *et al*., 2019). However, excessive managerial ownership may lead to entrenchment, reducing accountability and potentially harming firm value (Naciti, 2019).

Institutional ownership has the ability to monitor corporate management, reducing agency costs and consequently improving company performance (Boone & White, 2015). Independent commissioners and audit committees are integral components of GCG aimed at reducing agency problems. Independent commissioners ensure unbiased oversight of managerial activities. However, their effectiveness depends on their expertise and independence from management influence (Biçer & Feneir, 2019; W. I. L. Ningsih *et al*., 2023)

Audit committees, composed of professionals skilled in financial reporting, play a critical role in ensuring transparency and compliance with accounting standards.

Despite the theoretical robustness of these mechanisms, empirical findings are mixed. For example, (Lin & Fu, 2017; Musallam *et al*., 2019) found a impact of governance mechanisms on firm value. While, (Arsal, Badollahi, *et al*., 2024; Naciti, 2019; Riyadh *et al*., 2023) shown no significant influence on firm value. These inconsistencies suggest that the effectiveness of governance mechanisms may vary across contexts, influenced by factors such as industry dynamics and regulatory environments.

Profitability and Firm Value

Profitability remains a cornerstone of firm valuation, acting as a signal of financial health and growth potential. High profitability indicates efficient resource utilization and robust operational capabilities, which are critical for attracting investor confidence (Mahrani & Soewarno, 2018). Metrics like Return on Assets (ROA) are commonly employed to assess profitability. ROA reflects a company's ability to generate returns from its asset base, making it a reliable indicator of managerial efficiency

The relationship between profitability and firm value is well-documented. Studies (Alzoubi, 2018; García *et al*., 2012)) demonstrate that higher profitability correlates positively with firm value, as measured by Tobin's Q. This is because profitability enhances dividend-paying capacity and reinvestment potential, aligning with shareholder interests. However, Baihaqqi *et al*., (2023) argue that the impact of profitability may be contingent on external factors like market conditions and investor sentiment.

While profitability generally supports firm valuation, excessive focus on short-term profits can lead to myopic decision-making. Companies may underinvest in innovation or sustainability initiatives,. Such as a balanced approach that integrates profitability with strategic investments in sustainable practices is essential. emphasize that firms combining strong financial performance with environmental responsibility tend to achieve superior valuations (Krechovská & Procházková, 2014)

Carbon Emission Disclosure

Carbon emission disclosure has emerged as a vital dimension of corporate transparency in the era of climate change. By voluntarily reporting their carbon footprints, companies signal their commitment to environmental stewardship, potentially enhancing their reputational capital (Krechovská & Procházková, 2014; Ludwig & Sassen, 2022).

The theoretical underpinning of carbon disclosure lies in legitimacy theory, which posits that companies must align their practices with societal expectations to secure legitimacy (Deegan *et al*., 2002). In the Indonesian context, where carbon disclosure remains largely voluntary, companies engaging in such practices may gain a competitive edge by appealing to socially conscious investors. However, the extent to which carbon disclosure influences firm value remains contentious. (Cao *et al*., 2022; Hardiyansah & Agustini, 2020; Kurnia *et al.*, 2021) found a positive correlation, suggesting brings a competitive advantage for firms to create value.

Carbon disclosure is not without challenges. Companies face difficulties in accurately quantifying emissions and adhering to global reporting standards. Moreover, greenwashing—where firms exaggerate their environmental achievements—can undermine the credibility of disclosures (Cao *et al*., 2022). Thus, effective carbon disclosure requires robust internal systems for data collection and verification, coupled with adherence to frameworks like the Global Reporting Initiative (GRI).

The strategic value of carbon disclosure lies in its ability to mitigate risks associated with climate change, including regulatory penalties and shifting consumer preferences. The firms proactively managing their carbon footprints are better positioned to adapt to evolving market demands, ultimately enhancing their long-term sustainability and valuation (Noor & Ginting, 2022).

Hypotheses:

1. Good Corporate Governance, proxied by managerial ownership, institutional ownership, independent commissioners, and audit committees, significantly influences firm value.
2. Profitability positively impacts firm value.
3. Carbon emission disclosure significantly affects firm value.

METHOD

Data Collection

The study focuses on 11 mining companies listed on the IDX. The selection criteria for these companies include consistent listing on the IDX throughout the study period (2019-2022) and availability of relevant financial and governance data. Data were collected from annual reports, financial statements, and sustainability reports available on the IDX and company websites.

Variables

1. Dependent Variable:

Firm Value: Measured using Tobin's Q, which is calculated as the market value of a company divided by the replacement value of its assets.

2. Independent Variables:

- Good Corporate Governance (GCG): Assessed through indicators such as managerial ownership (MO), institutional ownership (IO), the presence of independent commissioners (IC), and the effectiveness of audit committees (AC).
- Profitability: Evaluated using Return on Assets (ROA) as indicators of a company's ability to generate profits from its assets and equity, respectively.
- Carbon Emission Disclosure: Measured by the extent and quality of carbon emission information disclosed in sustainability reports, using a scoring system based on the Global Reporting Initiative (GRI) standards.

RESULT

Descriptive Statistics

The descriptive statistics of the dataset provide valuable insights into the variables under study. Good Corporate Governance show the average MO was 2.39%, indicating low managerial ownership in the mining sector. IO averaged 62.88%, showing a stable and significant presence of institutional investors. The proportion of IC averaged 41.91%, and the number of AC members averaged 3.59, indicating a centralized distribution around the mean. ROA averaged 11.95%, with a standard deviation of 13.385%, indicating variability in profitability among companies. The average CED score was 45.81%, with a standard deviation of 26.047%, showing significant variability in disclosure levels. Also, Tobin's Q averaged 1.1505, with a standard deviation of 0.34141, indicating fluctuations in firm value. These figures highlight the diverse governance and financial characteristics within the sample.

Table 1: Descriptive statistics

Variables	N	Min	Max	Mean	SD
MO	44	0,00	0,50	0,0239	0,08546
IO	44	0,10	0,92	0,6288	0,17620
IC	44	0,20	0,75	0,4191	0,13203
AC	44	3,00	6,00	3,5909	0,78705
ROA	44	0,00	0,58	0,1195	0,13385
CED	44	0,05	0,95	0,4581	0,26047
Tobin’s Q	44	0,60	2,00	1,1505	0,34141

Assumption Testing

Normality, multicollinearity, and auto correlation tests were conducted as prerequisites in the regression analysis (Chen & Popovich, 2011). Firstly, the normality test results showed that the significance value (Sig.) was 0.200, which is greater than 0.05, indicating that the residuals are normally distributed and thus suitable for further parametric analysis. Secondly, multicollinearity tests revealed ed that all variables had variance inflation factor (VIF) values < 10 and tolerance values > 0.1, indicating the absence of harmful multicollinearity. Specifically, the VIF values for MO

(VIF = 1.130), IO (VIF = 1.390), IC (VIF = 1.163), AC (VIF = 1.988), ROA (VIF = 1.055), and CED (VIF = 1.230) are well below the recommended thresholds, while the tolerance values were also all above 0.1, further supporting the no multicollinearity conclusion. Finally, the Durbin-Watson value of 1,852 indicates the absence of autocorrelation.

Regression Analysis

The study model [Eq. 1] hypothesizes that firm value will stand at 1.928 when all the predictor variables in the model remain unchanged. However, a 1% increase in each of the predictor variates will lead to the following effects: MO (-0.789), IC -1.305), AC(-0.148), will slightly decrease firm value, IO (-0.030) will slightly decrease firm value. However, IO (0.168), ROA (1.067), and CED (0.190) increase firm value by various magnitudes. The error term (*e*) accounts for unexplained variance in firm value.

$Y = \alpha + \beta MO + \beta IO + \beta IC + \beta AC + \beta ROA + \beta ROE + e$ ..... [Eq. 1]

$\therefore Y = 1.928 - 0.789MO + 0.168IO - 1.305IC - 0.148AC + 1.067ROA + 0.190CED + e$

The hypothesis test results in Table 2 reveal that MO does not significantly affect firm vallue (H1.1: β = -0.789, *t* = -1.670, *p* = 0.103). Similarly, IO show a non-significant positive effect on firm value (H1.2: β 0,168, *t* = 0.662, *p* = 0.513). Although IC has a significant negative effect on firm value (H1.3: β = -1.305, *t* = -4.207, *p* = 0.000). Also, AC have significant negative effect on firm value (H1.4: β = -0.148, *t* = 2.805, *p* = 0.008). However, ROA has a significant positive effect on firm value (H2: β = 1.067, *t* = 3.659, *p* = 0.001). Otherwise, CED does not significantly impact on firm value (H3: β = 0.190, *t* = 1.176, *p* = 0.247).

Table 2: Multiple Regression

Variables	B	t	Sig.
(Constant)	1.928	6.702	0.000
MO	-0.789	-1.670	0.103
IO	0.168	0.662	0.512
IC	-1.305	-4.207	0.000
AC	-0.148	-2.805	0.008
ROA	1.067	3.659	0.001
CED	0.190	1.176	0.247

Finally, the model test results indicate a strong positive correlation between the independent and dependent variables, with a correlation coefficient R = 0.736. The R^2 = 0.542 suggests that approximately 73.6% of the variance in firm value is explained by MO, IO, IC, AC, ROA, and CED. The Adj. R^2 = 0.542, indicates that about 54.2% of the variance in firm value is explained by the model after accounting for the number of predictors.

DISCUSSION

The findings of this study offer nuanced insights into the interplay between governance, profitability, and carbon emission disclosure in influencing firm value. The significant negative effect of independent commissioners and audit committees on firm value challenges the traditional perception of these governance mechanisms as universally beneficial. While independent commissioners are expected to provide unbiased oversight, their influence in the mining sector may be constrained by limited industry-specific expertise or inadequate independence from management influence (Musallam *et al*., 2019; Sampurna & Romawati, 2020), the mere presence of governance structures does not guarantee effective oversight (S. S. Ningsih *et al*., 2024; Vijayakumaran & Vijayakumaran, 2019).

Profitability emerged as a robust positive determinant of firm value, reinforcing its centrality in corporate valuation. The significant coefficient of 0.30 underscores the critical role of financial performance in shaping investor perceptions. This aligns with Kurnia *et al*., (2020), who demonstrated that profitability metrics like ROA serve as reliable indicators of operational efficiency and managerial effectiveness. However, the emphasis on short-term profitability could potentially overshadow long-term investments in innovation and sustainability (Arsal, Badollahi, *et al*., 2024; Arsal, Dewisari, *et al*., 2024).

Carbon emission disclosure, despite its theoretical significance, showed no substantial impact on firm value in this study. This finding line with studies (Musallam *et al*., 2019; Sampurna & Romawati, 2020) that the voluntary nature of such disclosures in Indonesia limits their perceived credibility. Moreover, the prevalence of greenwashing, further undermines the efficacy of carbon disclosure as a tool for enhancing firm value. To address these challenges (Cao *et al*., 2022), regulatory frameworks need to evolve to standardize disclosure practices and ensure their reliability.

Institutional ownership demonstrated a weak positive effect on firm value, suggesting that institutional investors play a modest role in enhancing governance quality. The monitoring capabilities of institutional investors (Lin & Fu, 2017). However, the effectiveness of institutional oversight may vary depending on the concentration of ownership and the alignment of interests between institutional investors and minority shareholders (Mahrani & Soewarno, 2018).

The absence of a significant relationship between managerial ownership and firm value challenges the traditional view of managerial ownership as a mechanism to align the interests of managers and shareholders. The excessive managerial ownership could lead to entrenchment, reducing accountability and potentially harming firm value (Boone & White, 2015). This underscores the need for a balanced approach to

managerial ownership that optimizes alignment without compromising accountability.

CONCLUSION

This study provides empirical evidence on the interplay between governance, profitability, and environmental responsibility in shaping firm value within Indonesia's mining sector. The findings suggest prioritizing profitability and refining governance practices to enhance market perceptions. Policymakers and corporate leaders should also foster a culture of transparency and environmental accountability, aligning with global sustainability goals. Future research could explore sector-specific dynamics and the long-term implications of voluntary disclosures.

LIMITATIONS

This study has several limitations that consideration. First, the sample size was limited to 11 mining companies listed on the Indonesia Stock Exchange, potentially restricting the generalizability of the findings to other sectors or larger populations. Second, the study relies on secondary data derived from annual reports and sustainability disclosures. While these sources provide valuable insights, they may not fully capture qualitative aspects such as managerial intent or stakeholder perceptions. Third, the voluntary nature of carbon emission disclosures in Indonesia introduces variability in reporting standards, potentially affecting the reliability of the data. Lastly, the study's cross-sectional design limits its ability to establish causality. Longitudinal studies that track changes over time could provide more robust insights into the causal relationships among governance, profitability, carbon disclosure, and firm value.

FUTURE RESEARCH

- Expanding the sample size and including diverse industries to enhance external validity.
- Future studies could incorporate primary data collection methods, such as interviews or surveys, to gain a deeper understanding of the underlying dynamics.
- Explore the impact of mandatory disclosure regulations on the relationship between carbon emission disclosures and firm value.
- Investigate potential moderating or mediating factors, such as corporate culture, regulatory changes, or economic conditions, to develop a more comprehensive framework

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