



The Effect of ESG on Bank Performance: The Moderating Role of Foreign Ownership

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Citation: Serly., Tang, S., & Duha, N. C. (2026). The Effect of ESG on Bank Performance: The Moderating Role of Foreign Ownership. *Gorontalo Accounting Journal*, 9(1), 25-35. DOI: [10.32662/gaj.v9i1.4661](https://doi.org/10.32662/gaj.v9i1.4661)

Artikel info

Artikel history:

Received: 20-01-2026

Revised: 26-02-2026

Accepted: 31-03-2026

Abstract. *This study aims to analyze the impact of ESG on bank performance as measured by Return on Assets (ROA), Return on Equity (ROE), and GRI disclosure index with foreign ownership as a moderator. The research sample uses data from companies engaged in the banking sector in Indonesia with an observation period from 2019 to 2023. The research approach used is moderation regression analysis with secondary data from annual reports and sustainability reports. This study finds that foreign ownership can strengthen the positive influence of ESG on bank performance. This indicates that the involvement of foreign investors can strengthen the implementation of sustainability practices through better external oversight mechanism.*

Abstrak. Penelitian ini bertujuan untuk menganalisis dampak dari ESG terhadap kinerja bank yang diukur melalui tingkat Return on Assets (ROA), tingkat Return on Equity (ROE), serta indeks pengungkapan GRI dengan kepemilikan asing sebagai moderasi. Sampel penelitian menggunakan data perusahaan yang bergerak pada sektor perbankan di Indonesia dengan periode observasi dari tahun 2019-2023. Pendekatan penelitian yang digunakan adalah analisis regresi moderasi dengan data sekunder yang berasal dari laporan tahunan serta laporan keberlanjutan bank. Penelitian ini menemukan bahwa kepemilikan asing mampu memperkuat pengaruh positif ESG terhadap kinerja bank. Hal ini mengindikasikan bahwa keterlibatan investor asing dapat memperkuat penerapan praktik keberlanjutan melalui mekanisme pengawasan eksternal yang lebih baik.

Keywords:

*Environmental, Social,
and Governance (ESG);
Bank Performance;
Foreign Ownership*

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Introduction

After various global crises such as the 2008 financial crisis and the COVID-19 pandemic, awareness of sustainability issues has increased (Zhou et al., 2024). These conditions indicate that economic instability, environmental degradation, and social issues have a tangible impact on business performance and continuity (J. Kim et al., 2022). This has shifted the corporate perspective from focusing on short-term profits toward creating long-term value through practices in environmental, social, and corporate governance (ESG) aspects (Zumente & Bistrova, 2021).

Ruan and Liu (2021) emphasized that ESG practices now play a critical role in decision-making processes and capital market development. ESG practices have become part of corporate strategies to maintain competitiveness, attract investors, and ensure sustainable performance as they relate to the company's image and reputation (Harymawan et al., 2021). Consequently, many companies now prioritize responsibility for environmental, social, and governance (ESG) aspects as a concrete manifestation of concern for these issues (Cho, 2022; Gupta, 2024). In developing countries, the banking sector plays a crucial role in driving profitability, good reputation, and sustainable development (ElBannan, 2015; Nizam et al., 2019). Environmental and social risks faced by banks originate not only from internal operations but also from financing activities. Financing projects with potential environmental harm can affect the bank's reputation and performance, thereby positioning banks to allocate funding to sectors focused on sustainability (Bātae et al., 2021). Based on Circular Letters from the Financial Services Authority (OJK) through POJK Number 51/POJK.03.2017 and 16/SEOJK.04/2021, banks in Indonesia are increasingly required to actively manage and disclose ESG risks in a transparent manner. This is due to regulators and supervisors paying greater attention to the impact of ESG risks on financial sector stability (Gutiérrez-Ponce & Wibowo, 2023). Additionally, engaging with the public can build a trusted business image that cares about the safety and welfare of employees and customers (Bātae et al., 2021).

The presence of foreign ownership is believed to bring a positive influence to companies because it introduces better business practices from their home organizations and can optimize and enhance corporate governance (Al Amosh & Khatib, 2022). This is because most foreign investors are independent and experienced in corporate management, enabling them to actively monitor and prevent managerial actions that may hinder company growth (Lee, 2022). Generally, foreign investors are also oriented toward long-term profits, making potential risks arising from ESG aspects a primary focus (Guo & Zheng, 2021).

Foreign investors do not have direct access to daily operational activities, so corporate transparency in reporting is necessary to ensure information accuracy and build trust in management (Bose et al., 2024). Moreover, foreign investors encourage management to be actively involved in corporate social responsibility activities to foster stronger commitments to social responsibility (Setiawan et al., 2021). This commitment not only enhances reputation but also attracts socially-conscious customers and builds long-term relationships with stakeholders (Katenova & Qudrat-Ullah, 2024).

The main objective of this study is to examine the effect of ESG on bank performance in Indonesia with foreign ownership as a moderating variable. Proper ESG implementation can enhance reputation, customer trust, and promote better financial performance. However, foreign ownership may moderate the relationship between ESG and bank performance, where banks owned by foreign investors are more likely to adopt stricter ESG practices, thereby improving performance. Understanding the interaction between ESG, bank performance, and foreign

ownership is therefore crucial in determining effective strategies to enhance banking sector performance.

This study contributes to the literature by adding new insights on the relationship between ESG implementation and bank performance in Indonesia, which remains relatively limited compared to the non-financial sector. Moreover, the study emphasizes the role of foreign ownership as a moderating variable in this relationship. It shows that foreign ownership not only enhances competitiveness through foreign capital but also strengthens the impact of ESG practices on financial performance. These findings can guide the banking sector in considering foreign ownership as a strategic component in formulating more effective and sustainable ESG policies.

The Effect of ESG on Bank Performance

With growing awareness of sustainability, investment processes increasingly consider ESG practices in assessing corporate performance, as stakeholders recognize that good ESG disclosure can improve operational performance, yield higher returns, and reduce firm-specific risks (Caporale et al., 2022; Shaikh, 2021).

The environmental aspect depends heavily on emissions and carbon footprint, so implementing ESG in companies may increase additional costs due to environmental investments, such as reducing carbon emissions, using renewable energy, and preventing air and water pollution (Crespi & Migliavacca, 2020). However, Menicucci and Paolucci (2023) argued that environmental activities can positively impact a bank's competitiveness because they are associated with higher asset and capital returns and are considered efficient in resource utilization, providing competitive advantages from the stakeholders' perspective.

The social aspect considers legal and normative impacts regarding workers' rights and managers' and investors' perspectives on social issues, making CSR a relevant issue for stakeholders (Coelho et al., 2023). Related studies explain that CSR can strengthen stakeholder legitimacy, increasing trust from the public, investors, and shareholders, which in turn drives better performance (Anita & Amalia, 2021; Belasri et al., 2020).

In ESG activities, corporate governance must be emphasized to ensure all policies are achieved. Implementing an effective corporate governance structure can drive improved bank financial performance (Tanaka et al., 2024). Therefore, optimizing the number of independent commissioners and board directors is important, as they can influence decision-making processes and prevent conflicts of interest among directors (Chen et al., 2021). Good corporate governance ensures that stakeholders' interests are fairly represented in decision-making processes (Serly et al., 2023).

H1: ESG has a positive relationship with Bank Performance

The Effect of ESG on Bank Performance with Foreign Ownership as a Moderator

Amidjaya and Widagdo (2020) stated that the presence of foreign ownership is believed to positively influence companies because better business practices from their home organizations will be applied. Additionally, foreign ownership provides effective external monitoring of managerial activities, making companies more disciplined in decision-making and reducing the risk of future bankruptcy (Kim et al., 2020). Saini and Singhania (2019) found that the relationship between social and environmental disclosure and firm performance is negatively moderated because most foreign companies prioritize financial profit over other factors. However, Kouzez et al. (2024) argued that high involvement in ESG activities can improve bank performance by gaining legitimacy in foreign markets and enhancing their international reputation.

H2: Foreign Ownership strengthens the relationship between ESG and Bank Performance

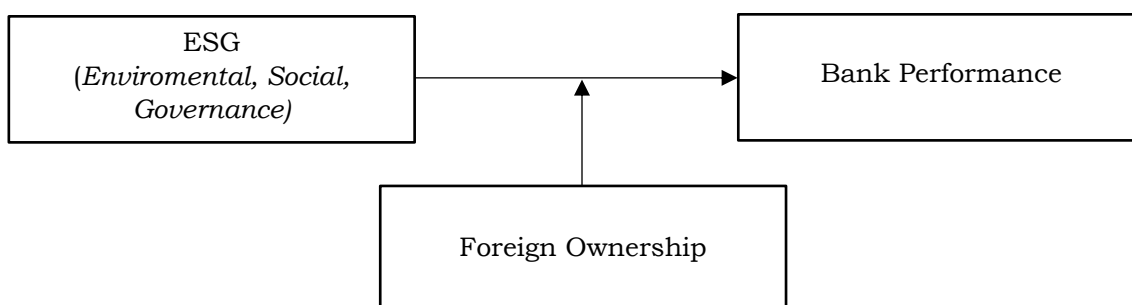


Figure 1. Research Model

Research Method

This study uses a quantitative approach focusing on the effect of ESG on Bank Performance, with foreign ownership serving as a moderating variable. The sample for this study was taken from the financial statements and sustainability reports of banking sector companies listed on the Indonesia Stock Exchange (IDX) from 2019 to 2023. The following are the measurements of the research variables:

Table 1. Research Variables and Measurements

Variable Name	Measurement
Dependen	
<i>Return on Asset</i> (ROA)	A ratio used to determine the extent to which a company can generate net income from its total assets. The higher the ROA, the more efficient the company is in utilizing all its assets to generate profits. This ratio is calculated by dividing net income after tax by total assets (Baselga-Pascual & Vähämaa, 2021).
<i>Return on Equity</i> (ROE)	Measures how effectively a company generates returns to shareholders on the invested capital. ROE is calculated by dividing net income after tax by total equity (Baselga-Pascual & Vahamaa, 2021).
Independent	
ESG	Calculated based on the GRI index disclosed in the sustainability report. This variable uses a dummy scale (1 if disclosure meets GRI indicators, 0 if not), then summed to produce the total ESG score (Rahman et al., 2023).
Moderating	
Foreign Ownership	Reflects the percentage of participation and involvement of foreign investors in the shareholding composition. Foreign ownership is calculated by dividing the number of shares held by foreign investors by the total outstanding shares of the company (Zarefar et al., 2024).

Result and Discussion

Descriptive Statistics Test

Table 2 presents the data characteristics of all research variables, consisting of ROA, ROE, ESG, and FO, with a total of 225 observations.

Table 2. Descriptive Statistics Results

	N	Mean	Standard Deviation	Minimum	Maximum
ROA	225	-0.001	0.063	-0.803	0.108
ROE	225	0.026	0.188	-1.503	1.414
ESG	225	0.400	0.339	0.000	0.943
FO	225	0.340	0.387	0.000	0.997

Source: Processed Data, 2025

The descriptive statistics show that company profitability measured using ROA is relatively low and varies slightly among the sample, as indicated by an average ROA of -0.001 with a standard deviation of 0.063. The minimum ROA of -0.803 and maximum of 0.108 indicate a wide range of profitability levels across companies.

The ROE variable has an average of 0.026 with a standard deviation of 0.188, meaning profitability based on equity returns is also relatively low but shows greater variation compared to ROA. The minimum value of -1.503 indicates that some companies experienced significant losses, while the maximum of 1.414 reflects high returns in certain companies.

Meanwhile, ESG has an average of 0.400 with a standard deviation of 0.339, indicating a moderate level of disclosure. Values range from 0.000 to 0.943, reflecting differences in ESG adoption among companies. Lastly, foreign ownership (FO) has an average of 0.340 with a standard deviation of 0.387, suggesting that foreign ownership in the sample companies is relatively low to moderate. Minimum and maximum values range from 0.000 to 0.997, indicating that in some cases, foreign ownership is nearly complete.

Pearson Correlation Test

Table 3. Pearson Correlation Results

	ROA	ROE	ESG	FO
ROA	1.000			
ROE	0.005 (0.945)	1.000		
ESG	0.041 (0.537)	0.104 (0.121)	1.000	
FO	0.084 (0.210)	-0.013 (0.851)	-0.057 (0.396)	1.000

Source: Processed Data, 2025

The correlation test results indicate that ROA does not have a significant relationship with other variables, with a correlation level below 1%. This suggests that profitability measured by ROA has no linear relationship with equity-based profitability, ESG practices, or foreign ownership. Similarly, ROE does not have a significant relationship with ESG or foreign ownership (FO), indicating that profitability measured by ROE does not strongly correlate linearly with ESG practices and foreign ownership. Meanwhile, the relationship between ESG and foreign

ownership (FO) shows a negative and insignificant correlation, suggesting that foreign ownership levels do not meaningfully relate to ESG implementation in companies.

The Effect of ESG on Return on Asset (ROA): Foreign Ownership as Moderator

Table 4. Regression Results

	(1) ROA	(2) ROA	(3) ROA
ESG	0.006 (1.39)	0.007 (1.46)	-0.002 (-0.37)
FO		0.005 (1.02)	-0.006 (-0.79)
ESGXFO			0.028** (2.56)
_cons	0.004 (1.30)	0.003 (0.69)	0.006 (1.42)
Year FE	Yes	Yes	Yes
F	1.903	1.590	3.150
r2_a	0.026	0.025	0.035
N	225	225	225

Source: Processed Data, 2025

In model (1), the ESG variable has a positive coefficient of 0.006 with a t-statistic of 1.39, although it is not statistically significant. A similar result is observed in model (2), where the ESG coefficient is 0.007 ($t = 1.46$). This indicates that implementing good environmental, social, and governance practices has not yet had a direct impact on bank performance measured by asset efficiency. This may occur because ROA measures short-term impacts of operational activities, whereas ESG activities typically require significant upfront costs, such as environmental investments, employee training, and governance system improvements, with economic benefits realized in the long term (Basali, 2025; Pulino et al., 2022).

Additionally, the foreign ownership (FO) variable shows a positive coefficient of 0.005 ($t = 1.02$) and is not significant, indicating that individually, neither ESG nor foreign ownership significantly affects bank profitability.

In model (3), the ESG coefficient becomes negative at -0.002 ($t = -0.37$) and FO is -0.006 ($t = -0.79$), both still insignificant. However, when the interaction between ESG and foreign ownership (ESGXFO) is included, the interaction variable shows a positive coefficient of 0.028 with a t-statistic of 2.56, significant at the 5% level. This indicates that foreign ownership moderates the positive relationship between ESG and ROA, meaning the effect of ESG on profitability (ROA) strengthens as the proportion of foreign ownership increases.

The Effect of ESG on Return on Equity (ROE): Foreign Ownership as Moderator

Table 5. Regression Results

	(1) ROE	(2) ROE	(3) ROE
ESG	0.042** (2.11)	0.041** (2.06)	0.001 (0.05)
FO		-0.013 (-0.76)	-0.061** (-2.09)
ESGXFO			0.123*** (2.67)
_cons	0.025* (1.75)	0.030* (1.90)	0.047** (2.51)
Year FE	Yes	Yes	Yes

F	2.014	1.714	2.707
r2_a	0.023	0.021	0.040
N	225	225	225

Source: Processed Data, 2025

Based on Table 5, in model (1), ESG has a positive coefficient of 0.042 with a t-statistic of 2.11, significant at the 5% level ($p < 0.05$). This indicates that implementing ESG practices has a positive and significant effect on bank profitability. In other words, the greater the ESG implementation, the higher the ROE.

In model (2), results remain consistent, with ESG showing a positive and significant effect on ROE with a coefficient of 0.041 ($t = 2.06$). Meanwhile, foreign ownership (FO) has a negative coefficient of -0.013 ($t = -0.76$) and is not significant, indicating that foreign ownership alone does not significantly affect bank profitability.

In model (3), the ESG coefficient is 0.001 ($t = 0.05$), not significant, while FO shows a negative coefficient of -0.061 with a t-statistic of -2.09, significant at 5%. This indicates that foreign ownership negatively affects profitability when the interaction variable is included. However, the ESGxFO interaction variable shows a positive coefficient of 0.123 with a t-statistic of 2.67, significant at the 1% level ($p < 0.01$), indicating that foreign ownership positively moderates the relationship between ESG and ROE. The effect of ESG on profitability strengthens as the proportion of foreign ownership increases.

Regression analysis results show that the effect of Environmental, Social, and Governance (ESG) variables differs across the two performance indicators used in this study, providing partial support for hypothesis H1. In the initial model, ESG has a positive coefficient for ROA but is not statistically significant, confirming that ESG practices have not yet had a direct impact on bank performance measured by asset efficiency. This may occur because ROA measures short-term operational impacts, whereas ESG activities require substantial upfront costs with long-term economic benefits (Basali, 2025; Pulino et al., 2022).

Unlike ROA, the ESG test on ROE indicates that ESG implementation has a positive and significant impact on bank performance in terms of equity returns. Companies with a strong commitment to sustainability tend to improve long-term competitiveness, attracting more capital from investors, especially foreign investors, thereby enhancing equity value and profitability as reflected in ROE (Meng et al., 2023). Moreover, good governance minimizes managerial risks, increases transparency, and improves decision-making processes (Yuan et al., 2022). Consequently, companies with high ESG compliance tend to achieve more stable and profitable financial performance for shareholders (Parikh et al., 2023).

However, the analysis shows that the ESG and foreign ownership (FO) interaction variable has a positive and significant relationship with financial performance, measured by both ROA and ROE, supporting hypothesis H2. The presence of foreign ownership is expected to enhance financial performance through technology, good governance, and improved managerial discipline in banks (Othmani, 2022). Foreign investors from countries with strong ESG regulations and awareness tend to apply pressure for better governance and transparency practices. This pressure encourages companies to implement ESG policies substantially rather than merely complying with regulatory requirements (Fuadah et al., 2022).

Conclusions and Recommendations

The empirical results demonstrate that ESG has a significant positive impact on Return on Equity (ROE), but does not have a significant effect on Return on Assets (ROA). This finding reveals that the implementation of sustainability principles has a

greater influence on increasing equity value and investor confidence than on the efficiency of bank asset utilization. Meanwhile, the relationship between foreign ownership and bank performance is not significant, indicating that the presence of foreign investors has not yet produced a tangible impact on short-term bank profitability.

However, the interaction variable between ESG and foreign ownership shows a positive and significant relationship with bank financial performance. This is because the presence of foreign investors encourages banks to enhance transparency, accountability, and the implementation of sustainability practices in accordance with international standards. These conclusions suggest that effective ESG implementation in the banking sector is still influenced by ownership structure. In the banking context, the interaction between these two factors operates synergistically, enabling more efficient, stable, and long-term sustainability-oriented performance.

This study has several limitations, particularly in terms of scope, as it is limited to banking companies in Indonesia listed on the Indonesia Stock Exchange (BEI), as well as constraints in ESG and foreign ownership data. Therefore, future researchers are expected to expand the sample and observation period and include additional variables such as firm size, leverage, and liquidity (Albitar et al., 2020) to obtain more comprehensive results regarding the phenomenon under study.

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