

## The Role of Profitability as a Mediating Variable in the Relationship between Sustainability Reporting and Firm Value in Islamic Commercial Banks in Indonesia

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### Article Info

**Article History:**  
Received 10 September th,  
2025  
Revised 12 December th,  
2025  
Accepted 15 February th,  
2026  
Available online in 10 April  
2026

**DOI:**  
10.70095/alamwalv17i2

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### ABSTRACT

**Introduction:** This study addresses the inconsistency of prior empirical findings regarding the effect of sustainability reporting on firm value, particularly in the Islamic banking sector where financial indicators remain dominant in investment decisions. The significance of this research lies in providing a clearer understanding of how sustainability practices contribute to firm value. Therefore, this study aims to examine the role of financial performance as a mediating variable in the relationship between sustainability reporting and firm value in Islamic commercial banks in Indonesia.

**Methods:** This research employs a causal quantitative approach using panel data from 10 Islamic commercial banks over the 2022–2024 period. Data are obtained from annual reports, sustainability reports, and financial statements. The analysis was conducted using panel data regression and the Sobel test to examine the mediating effect.

**Results:** The findings indicate that sustainability reporting has a positive effect on financial performance. In addition, financial performance significantly enhances firm value and acts as a mediating variable in the relationship between sustainability reporting and firm value.

**Conclusion and suggestion:** The results confirm that sustainability practices contribute to firm value indirectly through financial performance. Therefore, Islamic commercial banks are encouraged to strengthen the quality of sustainability reporting as a strategic effort to improve firm value and maintain long-term performance.

**Keywords:** Sustainability Reporting, Financial Performance, Firm Value, Islamic Banking, ESG

**Paper type:**  
**Research paper**

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## INTRODUCTION

The development of Islamic Commercial Banks in Indonesia has shown increasingly complex dynamics in line with the growing demand for the implementation of sustainability principles in the financial industry. Regulatory policies issued by the Financial Services Authority through POJK No. 51/POJK.03/2017 require banks, including Islamic banks, to prepare and publish Sustainability Reporting as an instrument of transparency and accountability to stakeholders (Jajang et al., 2023). However, in practice, the implementation of sustainability reporting in Islamic commercial banks still faces structural and substantive challenges, particularly in terms of consistency, depth of disclosure, and its linkage to operational performance (Dewi & Muhyarsyah, 2025; Gutiérrez-Ponce & Wibowo, 2023). Investors in the Indonesian Islamic banking sector continue to rely primarily on conventional financial indicators such as profitability and efficiency in assessing firm value, rather than non-financial indicators derived from sustainability reporting (Purnamawati & Dautrey, 2025). This condition creates a gap between the normative objective of sustainability reporting as a tool for long-term value creation and market reality, which remains oriented toward short-term financial performance (Gutiérrez-Ponce & Wibowo, 2023). Previous studies also highlight that sustainability practices are closely linked to financial outcomes and firm performance (Alshehhi et al., 2018; Dewi & Muhyarsyah, 2025; Friede et al., 2015; Orazalin & Mahmood, 2021).

Empirical literature shows that the relationship between sustainability reporting and firm value remains inconclusive, particularly in the context of developing countries and Islamic banking. Several studies find that environmental, social, and governance disclosure does not significantly affect firm value, as the market has not fully responded to such non-financial information (Buallay, 2019; Lindawati et al., 2023). Stakeholder Theory assumes that positive stakeholder responses to sustainability practices will lead to increased firm value, yet this assumption is often not directly confirmed in the empirical context of Islamic commercial banks (Malik & Abidin, 2025). Recent studies instead highlight that financial performance plays a dominant role in bridging the relationship between sustainability disclosure and firm value (Dewi & Muhyarsyah, 2025). These theoretical and empirical limitations indicate a research gap that requires a more comprehensive examination of mediating variables.

Based on the gap between empirical evidence and prior literature, this study is designed to achieve several objectives relevant to the development of Islamic finance. First, it aims to analyze the effect of sustainability reporting on the financial performance of Islamic commercial banks in Indonesia, given that financial performance is a key indicator of operational sustainability and competitiveness (Puspitasari et al., 2025). Second, it seeks to examine the effect of financial performance on firm value, considering that profitability and efficiency remain the primary concerns of investors in evaluating Islamic banks (Al Azizah & Haron, 2024). Third, this study investigates the role of financial performance as a mediating variable in the relationship between sustainability reporting and firm value, in order to explain the indirect mechanism of value creation through sustainability practices (Qoda'ah & Abdurrahman, 2023).

The urgency of this study lies in the need to develop a more contextual conceptual framework to explain the relationship between sustainability reporting, financial performance, and firm value in Islamic commercial banks. From the perspective of Maqasid al-Shariah, sustainability practices are not only intended to comply with regulatory requirements but also to generate long-term economic and social benefits (Ejaz et al., 2025). Research by Nurfadia & Fitriah (2025) Nurfadhila & Fitriah (2026) shows that the implementation of Islamic corporate governance can promote more sustainable corporate social responsibility practices and

generate both social and economic impacts. However, without strong financial performance, sustainability reporting may be perceived as a cost burden rather than a source of added value (Nurfadia Putri et al., 2025). This study argues that financial performance functions as a legitimizing mechanism that converts sustainability signals into market trust and enhanced firm value (Saprudin et al., 2025). Examining the mediating role of financial performance is expected to contribute theoretically to the development of Stakeholder Theory in the context of Islamic banking, while also providing practical implications for bank management and regulators in designing more effective sustainability policies.

This study is based on the argument that sustainability reporting does not directly influence firm value but operates through financial performance as a mediating mechanism. This argument is grounded in Stakeholder Theory, which explains that firms gain stakeholder support through transparency and responsible practices, ultimately improving financial outcomes and firm value (Dewi & Muhyarsyah, 2025; Parmar et al., 2010). The novelty of this research lies in integrating sustainability reporting, financial performance, and firm value within the context of Islamic commercial banks by emphasizing the mediating role of financial performance. Unlike prior studies that focus on direct relationships, this study provides a more comprehensive explanation of the indirect mechanism through which sustainability practices create economic value.

## **LITERATURE REVIEW**

### **Stakeholder Theory**

Stakeholder Theory explains that a firm is not only accountable to shareholders but also to all stakeholders affected by its activities, including investors, employees, customers, government, and society. This theory emphasizes that a firm's success depends on its ability to create value and maintain balanced relationships with stakeholders through transparent and responsible business practices. In the context of sustainability, the implementation of sustainability reporting is viewed as a strategic mechanism to communicate a firm's economic, social, and environmental performance to stakeholders, thereby enhancing legitimacy, reputation, and economic support (Gutiérrez-Ponce & Wibowo, 2023).

### **Sustainability Reporting**

Sustainability reporting is a non-financial reporting instrument used by firms to disclose their economic, social, and environmental performance in an integrated manner to stakeholders. In the banking context, sustainability reporting functions as a transparency mechanism that explains how banking activities align with sustainability principles and responsible governance (Gutiérrez-Ponce & Wibowo, 2023). In Islamic banking, sustainability reporting is not only regarded as a regulatory requirement but also as a representation of Islamic ethical values that emphasize justice, balance, and social responsibility (Ejaz et al., 2025). Several studies highlight that sustainability reporting serves as a strategic communication tool that conveys a firm's long-term commitment to sustainability to investors and regulators (Malik & Abidin, 2025). (Malik & Abidin, 2025; Nobanee & Ellili, 2016; Platonova et al., 2016). However, its effectiveness depends heavily on the quality and depth of disclosure rather than mere administrative compliance (Lindawati et al., 2023). Therefore, sustainability reporting can be understood as a strategic reporting system that integrates financial and non-financial dimensions to create sustainable value.

In practice, sustainability reporting is manifested through various frameworks and disclosure dimensions that reflect corporate sustainability aspects. In the Indonesian banking

sector, sustainability reporting is generally categorized into environmental, social, and governance dimensions as regulated by POJK No. 51/2017 (Jajang et al., 2023). The environmental dimension includes environmental risk management, energy efficiency, and green financing, while the social dimension covers responsibilities toward customers, employees, and society. The governance dimension focuses on transparency, compliance, and the effectiveness of internal supervision. In Islamic banking, sustainability reporting is also associated with Sharia compliance disclosure and contributions to Islamic social objectives (Yusmaniarti et al., 2023). This categorization indicates that sustainability reporting is not a single concept but a multidimensional set of practices reflecting a firm's overall commitment to sustainability.

### **Financial Performance**

Financial performance is a primary indicator used to assess a firm's ability to manage resources efficiently and generate sustainable profits. In Islamic banking, financial performance reflects the effectiveness of banks in performing their intermediation function in accordance with Sharia principles (Aisyah & Roziqin, 2025). It also serves as a key signal for investors in evaluating the prospects and stability of banks (Al Azizah & Haron, 2024). Several studies indicate that financial performance has a more direct relationship with firm value compared to non-financial disclosures (Purnamawati & Dautrey, 2025). Therefore, financial performance can be considered the primary foundation for building investor confidence and creating firm value.

In this study, financial performance is proxied by Return on Assets (ROA), as this indicator best reflects management effectiveness in utilizing total assets to generate profits. ROA is widely used in banking research because it captures overall operational performance and indicates how efficiently banks optimize their managed assets (Qoda'ah & Abdurrahman, 2023). Moreover, ROA is considered more relevant in the banking sector compared to other profitability indicators, as banking operations heavily depend on productive asset management to generate income. The use of ROA also enables the assessment of managerial efficiency in utilizing available resources to support operational stability and sustainability (Dewi & Muhyarsyah, 2025). In the sustainability context, strong financial performance reflected in a high ROA indicates that banks possess better financial capacity to support sustainability programs and consistent ESG practices (Nurfadia Putri et al., 2025).

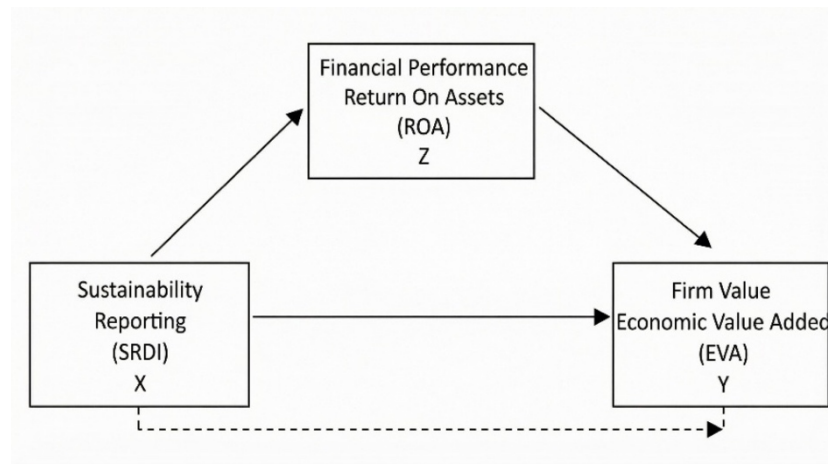
### **Firm Value**

Firm value represents market perceptions of a firm's performance, prospects, and risks in the long term. In the banking sector, firm value is closely associated with investor confidence in the stability and profitability of banks. It also reflects management's ability to balance financial performance and social responsibility (Malik & Abidin, 2025). In Islamic banking, firm value is not only viewed from a financial perspective but also from compliance with Sharia principles and social contributions (Handayani et al., 2025). Empirical studies indicate that Islamic investors still consider financial performance as the dominant factor in determining firm value. Thus, firm value can be understood as an integrative reflection of financial performance and market perceptions of corporate sustainability.

In quantitative research, firm value is generally measured using market-based indicators and economic value-added measures (Trisnawati et al., 2025). Economic Value Added (EVA) is used to measure the economic value created by a firm after accounting for the cost of capital (Rusmana & Sembiring, 2025). EVA is considered more capable of reflecting real value creation compared to conventional accounting indicators (Oktaviani et al.,

2025). In the context of Islamic banking, EVA is relevant as it considers capital efficiency within a sustainable financial framework (Kristanti et al., 2024). Empirical studies show that firm value is more responsive to financial performance than to sustainability disclosure directly. This highlights the importance of considering the mediating role of financial performance in measuring firm value.

The conceptual framework of this study is presented in Figure 1.



**Figure 1. Research Conceptual Framework**

Source: Author's Elaboration, 2026

Based on Stakeholder Theory, firms that are able to meet stakeholder expectations through transparent sustainability practices will gain economic support that enhances organizational performance. Sustainability reporting enables firms to build stronger relationships with investors, regulators, and society, thereby improving reputation and operational efficiency. Empirical studies also show that sustainability practices contribute to improved profitability through operational efficiency and better risk management (Dewi & Muhyarsyah, 2025). Empirical studies also confirm that sustainability and ESG practices contribute to both financial performance and firm value across various sectors (Awaysheh et al., 2020). (Awaysheh et al., 2020; Friede et al., 2015). Therefore, the first hypothesis is formulated as follows:

**H1:** Sustainability reporting has a positive effect on the financial performance of Islamic commercial banks.

Furthermore, from the perspective of Stakeholder Theory, strong financial performance reflects a firm's success in managing resources and fulfilling stakeholder expectations. Firms with high financial performance tend to gain greater investor confidence, which leads to higher firm value in the market (Al Azizah & Haron, 2024). Empirical studies also indicate that profitability is a key determinant of firm value in the banking sector. Therefore, the second hypothesis is formulated as follows:

**H2:** Financial performance has a positive effect on the firm value of Islamic commercial banks.

Moreover, sustainability reporting does not always directly affect firm value, as the market often evaluates sustainability through the financial performance generated by the firm. In this context, financial performance acts as a mechanism that converts sustainability practices into observable economic value for investors (Dewi & Muhyarsyah, 2025). Therefore, the relationship between sustainability reporting and firm value may occur indirectly

through improved financial performance. Based on this argument, the third hypothesis is formulated as follows:

**H3:** Financial performance mediates the effect of sustainability reporting on the firm value of Islamic commercial banks

## **METHOD**

This study employs a quantitative causal research design to examine the relationships between sustainability reporting, financial performance, and firm value. Quantitative research is used to analyze measurable variables through statistical testing in order to produce objective and generalizable findings (Triyono, 2015). In addition, this approach enables the identification of causal relationships among variables based on empirical data. This study utilizes secondary data obtained from published sources. The research object consists of Islamic Commercial Banks in Indonesia that consistently publish annual reports and sustainability reports. The data are collected from annual financial statements, sustainability reports, and official publications issued by the Financial Services Authority and the Indonesia Stock Exchange. The observation period covers 2022–2024, allowing for a comprehensive analysis of sustainability reporting practices and their impact on financial performance and firm value in the Islamic banking industry. Quantitative research is an approach used to analyze social phenomena through hypothesis testing involving variables that can be measured numerically and analyzed using statistical techniques (Triyono, 2015). This approach allows researchers to evaluate relationships between variables objectively based on available empirical data. This study uses secondary data obtained from previously published sources.

The object of this study is Islamic Commercial Banks in Indonesia that publish annual reports and sustainability reports during the observation period. The data are derived from annual financial reports, sustainability reports, and official publications issued by the Financial Services Authority and the Indonesia Stock Exchange. The observation period covers 2022–2024, allowing an analysis of the development of sustainability reporting practices and their impact on financial performance and firm value in the Islamic banking industry.

### **Population and Sampling Technique**

The population in this study includes all Islamic Commercial Banks operating in Indonesia during the observation period. Population refers to a set of research objects that possess characteristics relevant to the research objectives (Triyono, 2015). The sample is determined using a purposive sampling technique, which selects research objects based on specific criteria to ensure data relevance and completeness. The selected banks are those that operated consistently during the observation period, published both annual and sustainability reports, and provided complete data related to sustainability reporting, financial performance, and firm value. Based on these criteria, 10 Islamic Commercial Banks are selected as the research sample. With a three-year observation period, the total panel data used in this study consists of 30 observations. Population refers to the entire set of research objects that possess specific characteristics relevant to the research objectives (Triyono, 2015). The population in this study consists of all Islamic Commercial Banks operating in Indonesia during the observation period. Based on data from the Financial Services Authority, several Islamic banks operate fully within the national banking system.

The sampling technique used is purposive sampling, which selects samples based on specific criteria aligned with the research objectives. The criteria applied are as follows: First, Islamic Commercial Banks that operated consistently during the observation period. Second, banks that published annual reports and sustainability reports during the observation period. Third, banks that provided complete data related to the research variables, namely sustainability reporting, financial performance, and firm value. Based on these criteria, 10 Islamic Commercial Banks were selected as the research sample. With a three-year observation period, the total panel data analyzed in this study consists of 30 observations.

### Operational Variables

This study involves three main variables consisting of an independent variable, a mediating variable, and a dependent variable. Sustainability reporting serves as the independent variable and is measured using the Sustainability Reporting Disclosure Index, which reflects the proportion of disclosed sustainability items. Financial performance acts as the mediating variable and is proxied by Return on Assets, representing the efficiency of asset utilization in generating profits. Firm value is treated as the dependent variable and is measured using Economic Value Added, which reflects the firm's ability to create economic value after accounting for the cost of capital (Oktaviani et al., 2025). The operational definitions and measurement indicators of each variable are presented in Table 1. The variables used in this study consist of independent, mediating, and dependent variables. The independent variable is sustainability reporting, measured using the Sustainability Reporting Disclosure Index (SRDI). The mediating variable is financial performance, proxied by Return on Assets (ROA). The dependent variable is firm value, measured using Economic Value Added (EVA).

**Table 1. Table of Operational Variables**

Variable	Indicator	Scale
Sustainability Reporting (Independent)	SRDI = number of disclosed items / total standard items	Ratio
Financial Performance (Mediating)	ROA = Net Income / Total Assets	Ratio
Firm Value (Dependent)	EVA = NOPAT – (Cost of Capital × Invested Capital)	Ratio

Source: Author's Elaboration, 2026

### Data Analysis Method

The data analysis in this study applies a quantitative approach using panel data regression to examine the relationships among variables. Panel data analysis combines cross-sectional and time-series data, allowing for more robust estimation and better control of individual heterogeneity (Baltagi, 2021). The analysis is conducted using EViews statistical software.

The analysis begins with descriptive statistics to provide an overview of the characteristics of the research variables. Subsequently, panel data regression models are estimated using the Common Effect Model, Fixed Effect Model, and Random Effect Model. The selection of the most appropriate model is determined through the Chow test, Hausman test, and Lagrange Multiplier test. Data analysis in this study employs a quantitative approach to examine the effect of independent variables on the dependent variable and the mediating role within the research model. Data processing is conducted using EViews statistical software. The initial stage involves descriptive statistics to provide an overview of the

characteristics of the research data without making generalizations to the population. Furthermore, this study applies panel data regression models consisting of the Common Effect Model, Fixed Effect Model, and Random Effect Model. To determine the most appropriate model, several model selection tests are conducted, including the Chow test, Hausman test, and Lagrange Multiplier test.

The regression models used in this study are formulated as follows. The first model examines the effect of sustainability reporting on financial performance: The regression equations used in this study are as follows:

The first model examines the effect of sustainability reporting on financial performance:

$$ROA = \alpha + \beta_1 SRDI + \varepsilon \dots \dots \dots (1)$$

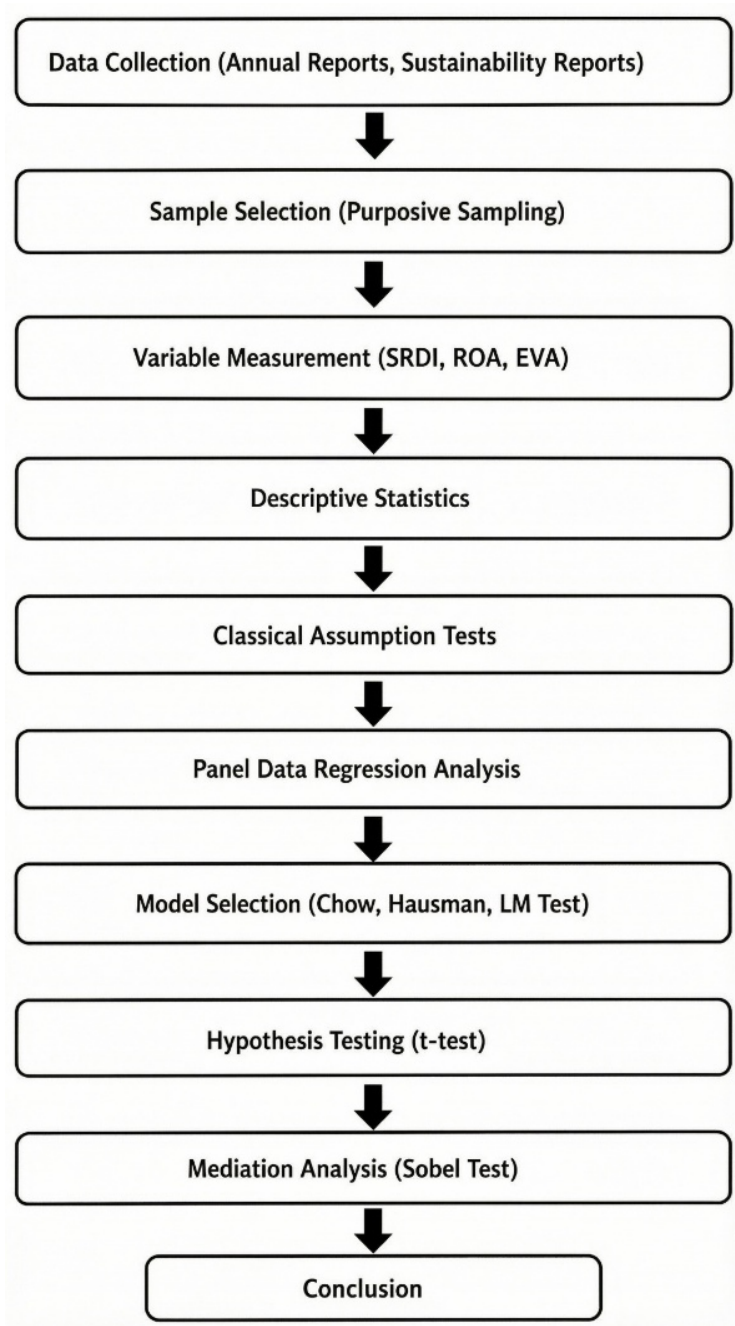
The second model examines the effect of sustainability reporting and financial performance on firm value:

$$EVA = \alpha + \beta_1 SRDI + \beta_2 ROA + \varepsilon \dots \dots \dots (2)$$

After determining the appropriate model, classical assumption tests are conducted to ensure the validity of the regression model. These include tests of normality, multicollinearity, heteroscedasticity, and autocorrelation. Hypothesis testing is performed using the t-test to evaluate the significance of each independent variable. A variable is considered significant if the probability value is less than or equal to 0.05. Furthermore, mediation analysis is conducted using the Sobel test to assess the indirect effect of sustainability reporting on firm value through financial performance. The Sobel test is widely used to examine mediation effects in causal models (Baltagi, 2021). The final stage of analysis involves calculating the coefficient of determination to evaluate the explanatory power of the model. After ensuring that all classical assumption tests are satisfied, the regression results can be interpreted with greater confidence. The normality test confirms whether the residuals are distributed normally, while the multicollinearity test ensures that there is no strong correlation among independent variables that could distort the estimation results. In addition, the heteroscedasticity test verifies the consistency of variance across observations, and the autocorrelation test checks for correlation between residuals over time. If these assumptions are met, the regression model is considered reliable and suitable for hypothesis testing. The results of the t-test then provide insight into the individual influence of each independent variable on the dependent variable, allowing researchers to identify which factors significantly affect firm value.

Furthermore, the mediation analysis using the Sobel test provides a deeper understanding of the indirect relationships within the model. This test evaluates whether financial performance acts as an intervening variable that transmits the effect of sustainability reporting on firm value. A significant Sobel test result indicates the presence of a mediation effect, either partial or full, depending on the direct relationship between variables. Finally, the coefficient of determination ( $R^2$ ) is used to measure how well the independent variables explain the variation in the dependent variable. A higher  $R^2$  value indicates a stronger explanatory power of the model, thereby reinforcing the robustness and overall validity of the research findings.

The overall research process is summarized in Figure 2.



**Figure 2. Research Flowchart**

Source: Author's Elaboration (2026)

After selecting the best regression model, classical assumption tests are conducted, including normality, multicollinearity, heteroscedasticity, and autocorrelation tests, to ensure that the regression model meets the required statistical assumptions. Hypothesis testing is carried out using the t-test to determine the effect of each independent variable on the dependent variable. An independent variable is considered to have a significant effect if the probability value (p-value) is less than or equal to the significance level of 0.05. Otherwise, if the probability value exceeds 0.05, the variable is considered not to have a significant effect. In addition, this study employs the Sobel test to examine the mediating role of financial

performance in the research model. This test determines whether financial performance significantly mediates the relationship between sustainability reporting and firm value. The final stage of analysis involves calculating the coefficient of determination ( $R^2$ ) to assess the extent to which the independent variables explain the variation in the dependent variable within the research model.

## RESULT AND ANALYSIS

### Descriptive Analysis of Variables

The analysis begins with descriptive statistics aimed at providing a general overview of the characteristics of each research variable. The variables analyzed include firm value proxied by Economic Value Added (EVA), sustainability reporting proxied by the Sustainability Reporting Disclosure Index (SRDI), and financial performance proxied by Return on Assets (ROA).

**Table 2. Descriptive Statistics of Variables**

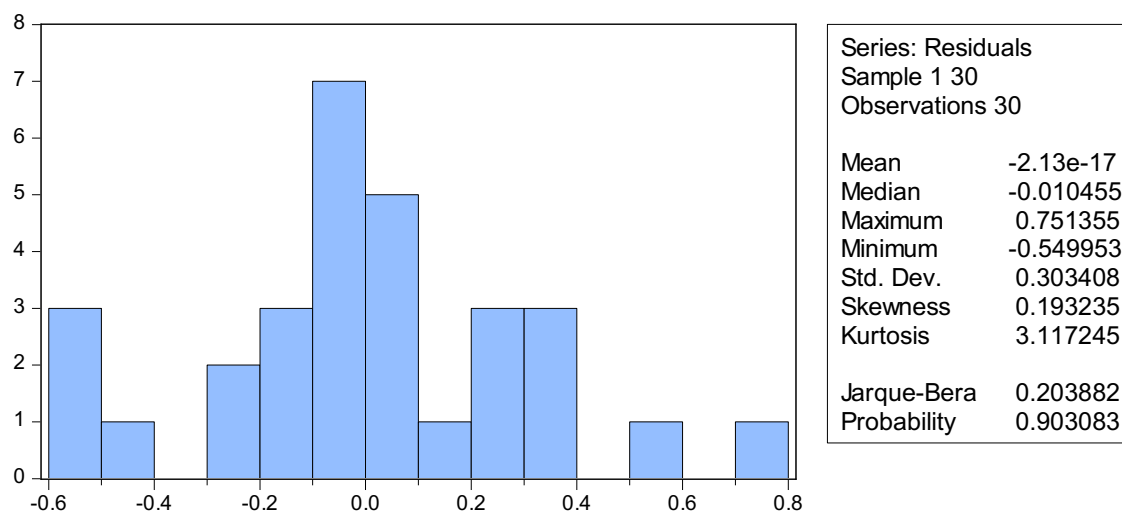
Variable	n	Minimum	Maximum	Mean
EVA	30	10247.00	14090548	1563409
SRDI	30	0.065934	0.505495	0.225641
ROA	30	-0.114700	0.113600	0.017160

Source: Processed Data Using EViews 12

Based on Table 2, the total number of observations is 30 panel data derived from 10 Islamic Commercial Banks over the 2022–2024 period. The descriptive results show that EVA has a minimum value of 10,247 and a maximum value of 14,090,548, with an average of 1,563,409. The SRDI variable ranges from 0.065934 to 0.505495, with a mean value of 0.225641. Meanwhile, ROA ranges from –0.114700 to 0.113600, with an average value of 0.017160. These results indicate that the level of sustainability reporting disclosure among Islamic commercial banks remains moderate, while financial performance and firm value exhibit considerable variation across banks and periods.

### Classical Assumption Tests

The next step involves testing classical assumptions to ensure that the regression model meets the criteria of a reliable estimator. In addition, the heteroscedasticity test is used to examine whether the variance of the residuals remains constant across all levels of the independent variables. A violation of this assumption may lead to inefficient estimates and biased standard errors. The autocorrelation test, on the other hand, is particularly relevant for time-series or panel data, as it detects correlations between residuals across observations. If all these classical assumptions are satisfied, the regression model can be considered appropriate for further analysis, including hypothesis testing and interpretation of results.



**Figure 2. Results of the Normality Test**

Source: Processed Data Using EViews 12

Based on the normality test results (Figure 32), the probability value is 0.903083, which is greater than the significance level of 0.05, indicating that the residuals are normally distributed. Furthermore, Table 3 presents the heteroscedasticity test results using the Glejser method, showing a probability value of Obs\*R-squared of 0.0908, which is also greater than 0.05. This indicates that the regression model does not suffer from heteroscedasticity.

**Table 3. Heteroskedasticity Test: Glejser**

F-statistic	2.570245	Prob. F (2,27)	0.0951
Obs*R-squared	4.798143	Prob. Chi-Square (2)	0.0908
Scaled explained SS	5.539992	Prob. Chi-Square (2)	0.0627

Source: Processed Data Using EViews 12

Based on the results of the heteroskedasticity test using the Glejser method, the values obtained are Prob. F = 0.0951, Prob. Chi-Square (Obs\*R-squared) = 0.0908, and Prob. Chi-Square (Scaled explained SS) = 0.0627. All probability values are greater than the significance level of 0.05, indicating that there is no evidence of heteroskedasticity in the regression model. Thus, it can be concluded that the residuals have constant variance (homoskedasticity), meaning that the model satisfies one of the key classical assumptions.

**Table 4. Heteroscedasticity Test Results (Glejser Test)**

	Coefficient	Uncentered	Centered
Variable	Variance	VIF	VIF
C	0.004061	1.232144	NA
SRDI	0.005974	2.314556	1.881698
ROA	0.005695	2.045271	1.881698

Source: Processed Data Using EViews 12

The multicollinearity test results in Table 4 show that all variables have Variance Inflation Factor (VIF) values below 10, specifically 1.881698 for both SRDI and ROA, indicating no high correlation among independent variables. In addition, the autocorrelation test results in Table 5 using the Breusch-Godfrey Serial Correlation LM Test show a Durbin-Watson value

of 1.991445 and a Chi-Square probability value of 0.5316, which is greater than 0.05. Therefore, the regression model does not exhibit autocorrelation issues.

**Table 5. Autocorrelation Test Results**

<b>Breusch-Godfrey Serial Correlation LM Test:</b>			
Durbin-Watson stat	1.991445		
Obs*R-squared	1.263797	Prob. Chi-Square (2)	0.5316

Source: Processed Data Using EViews 12

### Selection of the Best Regression Model

After all classical assumptions are satisfied, the next step is to determine the most appropriate panel data regression model.

**Table 6. Chow Test Results (Redundant Fixed Effects Test)**

Effects Test	Statistic	d.f.	Prob.
Cross-section F	1.253888	(9,18)	0.3250
Cross-section Chi-square	14.601106	9	0.1025

Source: Processed Data Using EViews 12

Based on Table 6, the Chow test results show a Cross-section Chi-square probability value of 0.1025, which is greater than 0.05. This indicates that the Common Effect Model is more appropriate than the Fixed Effect Model.

**Table 7. Hausman Test Results**

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	1.033737	2	0.5964

Source: Processed Data Using

The Hausman test results in Table 7 show a probability value of 0.5964, which is also greater than 0.05, indicating that the Random Effect Model is not preferable. Furthermore, the Lagrange Multiplier test results in Table 8 show a Breusch-Pagan probability value of 0.4834, which exceeds 0.05. These results confirm that the Common Effect Model is the most suitable model for this study.

**Table 8. Lagrange Multiplier Test Results**

	<b>Test Hypothesis</b>		
	Cross-section	Time	Both
Breusch-Pagan	0.062348	0.428868	0.491216
	(0.8028)	(0.5125)	(0.4834)

**Table 9. Common Effect Model Test Results (Model 1)**

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.056718	0.063726	-0.890035	0.3813
SRDI	0.167429	0.077294	2.166143	0.0393
ROA	0.798162	0.075467	10.57626	0.0000
R-squared	0.911571	Mean dependent var		0.270667
Adjusted R-squared	0.905020	S.D. dependent var		1.020304
S.E. of regression	0.314445	Akaike info criterion		0.618624
Sum squared resid	2.669642	Schwarz criterion		0.758744
Log likelihood	-6.279362	Hannan-Quinn criter.		0.663450
F-statistic	139.1644	Durbin-Watson stat		1.561229
Prob(F-statistic)	0.000000			

Source: Processed Data Using

The first regression results show that sustainability reporting (SRDI) has a coefficient of 0.167429 with a probability value of 0.0393, which is less than 0.05. This indicates that sustainability reporting has a positive and significant effect on firm value (EVA). In addition, financial performance (ROA) has a coefficient of 0.798162 with a probability value of 0.0000, indicating a positive and significant effect on firm value. Thus, Hypothesis 1 and Hypothesis 2 are accepted. The coefficient of determination ( $R^2$ ) of 0.911571 indicates that approximately 91.15% of the variation in firm value can be explained by sustainability reporting and financial performance, while the remaining 8.85% is influenced by other factors.

**Table 10. Common Effect Model Test Results (Model 2)**

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.034930	0.159443	-0.219074	0.8282
SRDI	0.701084	0.141101	4.968657	0.0000
R-squared	0.468565	Mean dependent var		0.307667
Adjusted R-squared	0.449585	S.D. dependent var		1.061358
S.E. of regression	0.787421	Akaike info criterion		2.424232
Sum squared resid	17.36088	Schwarz criterion		2.517646
Log likelihood	-34.36349	Hannan-Quinn criter.		2.454116
F-statistic	24.68755	Durbin-Watson stat		1.403960
Prob(F-statistic)	0.000030			

Source: Processed Data Using

Further testing examines the effect of sustainability reporting on financial performance. Based on Table 10, SRDI has a coefficient of 0.701084 with a probability value of 0.0000,

indicating a positive and significant effect on ROA. The  $R^2$  value of 0.468565 indicates that approximately 46.85% of the variation in financial performance is explained by sustainability reporting.

### Sobel Test

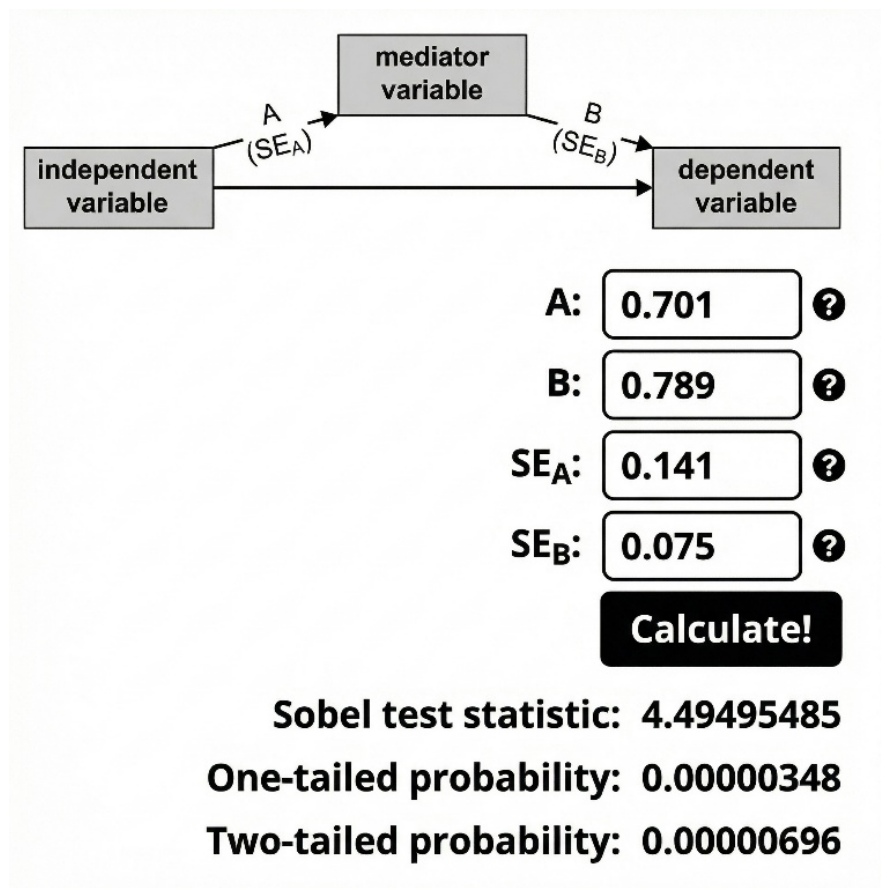


Figure 3. Sobel Test Results

Source: Processed Data Using The Sobel Test Calculator

The mediation effect is tested using the Sobel test. The results show a Sobel statistic value of 4.4949 with a two-tailed probability of 0.00000696, which is less than 0.05. This indicates that financial performance significantly mediates the relationship between sustainability reporting and firm value. Therefore, Hypothesis 3 is accepted. These results indicate that sustainability reporting not only has a direct effect on firm value but also an indirect effect through financial performance.

## DISCUSSION

### Effect of Sustainability Reporting on Financial Performance

The results indicate that sustainability reporting has a positive and significant effect on financial performance. This finding suggests that higher levels of sustainability disclosure contribute to improved operational efficiency and resource management in Islamic commercial banks. From an economic perspective, sustainability reporting reduces information asymmetry

between firms and stakeholders, thereby lowering transaction costs and enhancing stakeholder trust. This increased trust can improve access to funding and strengthen customer loyalty, ultimately leading to better financial performance. From the perspective of Stakeholder Theory, firms that actively disclose sustainability information are more likely to gain legitimacy and support from stakeholders, which enhances their operational effectiveness. This mechanism explains how sustainability practices translate into improved profitability. These findings are consistent with recent empirical studies that highlight the positive relationship between sustainability disclosure and financial performance (Dewi & Muhyarsyah, 2025; Gutiérrez-Ponce & Wibowo, 2023).

In the context of Islamic banking, sustainability reporting also reflects the implementation of Islamic corporate governance principles, which emphasize transparency, accountability, and social responsibility. These principles not only fulfill ethical obligations but also improve institutional credibility and financial outcomes. Therefore, sustainability reporting can be understood as both a compliance mechanism and a strategic tool for enhancing financial performance. The results show that sustainability reporting positively and significantly affects financial performance. This indicates that higher levels of sustainability disclosure are associated with better financial performance in Islamic commercial banks. From the perspective of Stakeholder Theory, firms that meet stakeholder expectations gain greater legitimacy and trust, which enhances operational efficiency and performance. Sustainability reporting functions not only as a transparency tool but also as a strategy to strengthen reputation and financial outcomes. These findings are consistent with Dewi and Muhyarsyah (2025), as well as prior studies highlighting the positive relationship between sustainability practices and financial performance (Alshehhi et al., 2018; Velte, 2017). From an Islamic economic perspective, sustainability practices are closely linked to Islamic corporate governance principles, which emphasize transparency, accountability, and social responsibility. The findings of Nurfadhila and Fitriah (2026) support this view, showing that Islamic corporate governance strengthens sustainable CSR practices and generates social and economic benefits.

### **Effect of Sustainability Reporting on Firm Value**

The findings show that sustainability reporting has a positive and significant effect on firm value. This indicates that investors perceive sustainability disclosure as a signal of long-term stability and lower risk. From an economic standpoint, sustainability reporting serves as a signaling mechanism that reduces uncertainty regarding future performance, thereby increasing investor confidence and firm valuation. According to Stakeholder Theory, firms that meet stakeholder expectations are more likely to receive stronger support from investors and society, which contributes to higher firm value. Sustainability reporting strengthens corporate reputation and reduces perceived risk, both of which are critical determinants of firm valuation. These results are in line with recent studies showing that sustainability practices positively influence firm value in the banking sector (Gutiérrez-Ponce & Wibowo, 2023; Malik & Abidin, 2025).

From an Islamic perspective, this relationship reflects the implementation of *maqasid al-shariah*, which emphasizes the creation of social and economic welfare. Sustainability reporting aligns business activities with ethical and social objectives, thereby enhancing both financial and non-financial value. The results indicate that sustainability reporting has a positive and significant effect on firm value. This suggests that improved sustainability disclosure enhances investor perception of long-term prospects, leading to increased firm value. In the context of Stakeholder Theory, firms that meet stakeholder expectations receive

stronger support from investors and society. These findings are consistent with Gutiérrez-Ponce and Wibowo (2023) and Malik and Abidin (2025). From an Islamic perspective, this reflects the implementation of Maqasid al-Shariah in achieving economic and social welfare. This finding is also supported by recent evidence in Islamic banking studies that confirms the role of profitability and sustainability disclosure in enhancing firm value.

### **Effect of Financial Performance on Firm Value**

The results demonstrate that financial performance has a positive and significant effect on firm value. This finding confirms that profitability remains a key determinant of firm valuation in Islamic banking. From an economic perspective, higher financial performance indicates efficient resource allocation and stable income generation, which reduces investment risk and increases expected returns for investors. Financial performance acts as a direct signal of a firm's ability to generate value, making it a primary factor in investment decision-making. According to Stakeholder Theory, firms that effectively manage resources are better able to meet stakeholder expectations, which strengthens market confidence and firm value. These findings are consistent with recent empirical evidence emphasizing the dominant role of financial performance in determining firm value (Al Azizah & Haron, 2024; Purnamawati & Dautrey, 2025). Thus, financial performance can be considered the most observable indicator of firm quality, directly influencing investor perception and market valuation.

The findings show that financial performance positively and significantly affects firm value. Higher profitability indicates better efficiency and stability, which increases investor confidence. This aligns with Stakeholder Theory, where effective resource management creates value for stakeholders. These findings are consistent with Al Azizah and Haron (2024), Purnamawati and Dautrey (2025). This result is also supported by previous studies that link sustainability practices with firm valuation through market perception and risk reduction (Awaysheh et al., 2020; El Ghouli et al., 2011).

### **The Mediating Role of Financial Performance**

The mediation analysis confirms that financial performance significantly mediates the relationship between sustainability reporting and firm value. This finding indicates that sustainability practices do not directly translate into firm value but operate through improved financial performance. From an economic perspective, sustainability reporting generates value by enhancing efficiency, reducing risk, and improving stakeholder trust, which are then reflected in financial performance. Financial performance serves as an intermediate mechanism that converts sustainability initiatives into measurable economic outcomes. Without strong financial performance, sustainability reporting may not be fully valued by the market. These findings support recent literature emphasizing the mediating role of financial performance in the relationship between sustainability disclosure and firm value (Dewi & Muhyarsyah, 2025; Rusmana & Sembiring, 2025).

From an Islamic perspective, this mechanism reflects a balance between ethical responsibility and economic performance, consistent with maqasid al-shariah. Sustainability practices contribute to social welfare, while financial performance ensures economic viability, both of which are essential for long-term value creation. The mediation test confirms that financial performance mediates the relationship between sustainability reporting and firm value. This indicates that sustainability practices enhance firm value both directly and indirectly through improved financial performance. Financial performance acts as a mechanism that translates sustainability practices into observable economic value for investors. These findings are consistent with Qoda'ah and Abdurrahman (2023) and Dewi and Muhyarsyah (2025).

From an Islamic perspective, this relationship reflects a balance between economic profit and social responsibility in line with Maqasid al-Shariah, emphasizing sustainable and equitable economic development. This mediating mechanism is also supported by prior literature emphasizing the role of financial performance in translating sustainability initiatives into economic value (Khan et al., 2016).

## **CONCLUSION**

This study reveals that sustainability reporting does not always exert a strong direct effect on firm value but demonstrates a more significant impact when mediated by financial performance. The findings show that an increase in the Sustainability Reporting Disclosure Index in Islamic Commercial Banks in Indonesia significantly improves financial performance, as reflected in Return on Assets, which subsequently contributes to higher firm value measured by Economic Value Added. These results indicate that sustainability reporting generates tangible economic benefits and should be viewed not merely as a compliance requirement but as a strategic instrument for enhancing firm performance and value creation. Theoretical and empirical contributions of this study lie in strengthening the understanding of the relationship between sustainability reporting, financial performance, and firm value in Islamic banking. This study provides empirical support for Stakeholder Theory by demonstrating that sustainability transparency enhances stakeholder trust through improved financial performance. It also contributes to Islamic economic literature by linking sustainability practices with maqasid al-shariah values, emphasizing the integration of ethical responsibility and economic performance. From a practical perspective, the findings offer important implications for Islamic bank management, regulators, and investors in designing strategies that integrate sustainability with financial performance to achieve long-term value creation.

Despite these contributions, this study has several limitations. The observation period is relatively short, covering only three years, and the analysis is limited to sustainability reporting and financial performance as the main determinants of firm value. These limitations may affect the generalizability of the findings. Future research is recommended to incorporate additional variables such as corporate governance quality, corporate reputation, and risk factors in Islamic banking. Further studies may also extend the observation period and apply more advanced analytical methods, such as structural equation modeling or moderation analysis, to provide a more comprehensive understanding of the relationship between sustainability practices and firm value. The most important finding of this study reveals a notable insight that provides a new perspective in Islamic finance research. Sustainability reporting does not always exert a strong direct effect on firm value but demonstrates a more significant impact when mediated by financial performance. The results show that an increase in the Sustainability Reporting Disclosure Index in Islamic Commercial Banks in Indonesia significantly improves financial performance, as reflected in Return on Assets. This improvement subsequently contributes to an increase in firm value, measured by Economic Value Added. These findings indicate that sustainability reporting is not merely a symbolic commitment to social and environmental issues but also generates tangible economic implications for firm performance. In the context of Islamic banking, sustainability should not be viewed solely as an ethical or regulatory requirement but as a strategic business approach that enhances operational efficiency and creates greater economic value. Therefore, sustainability reporting can be understood as a strategic instrument that strengthens

relationships with stakeholders while serving as a mechanism for firm value creation in the Islamic financial industry.

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