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ESG Performance and Governance: Implications for Conservatism and Cost of Equity

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ABSTRACT

This study examines the effects of Environmental, Social, and Governance (ESG) performance, managerial ownership, and profitability on the cost of equity and accounting conservatism among manufacturing firms listed on the Indonesia Stock Exchange during 2020–2024. Using purposive sampling, this study analyzes 98 firm year observations through panel data regression. The findings show that ESG performance positively affects accounting conservatism, indicating that firms with stronger sustainability practices tend to adopt more prudent financial reporting. In addition, managerial ownership negatively influences the cost of equity, suggesting that greater managerial shareholding reduces agency conflicts and investor risk perceptions. However, managerial ownership and profitability do not significantly affect accounting conservatism, while ESG performance, profitability, and accounting conservatism do not significantly influence the cost of equity. The findings suggest that sustainability practices and governance mechanisms play complementary roles in shaping reporting quality and financing decisions.

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1. INTRODUCTION

The increasingly dynamic pace of economic growth requires companies to continually adapt to intensifying business competition in order to sustain their operations and reinforce their competitive advantage (Sagita & Wibowo, 2025). In response to these challenges, stakeholders are increasingly demanding that companies demonstrate not only strong financial performance but also responsible and sustainable business practices (Zhou & Lei, 2025). Consequently, Environmental, Social, and Governance (ESG) performance has become an important consideration in assessing corporate quality, risk, and long-term value creation (Wulandari & Abdillah, 2025).

ESG performance is widely regarded as a mechanism for reducing information asymmetry and enhancing corporate transparency (Mao et al., 2024). Companies with strong ESG performance are generally expected to provide more comprehensive disclosures and demonstrate greater accountability to stakeholders, thereby reducing uncertainty regarding future business prospects (Thanatawee, 2023). Beyond its role in sustainability reporting, ESG performance may also influence the quality of financial reporting (Zhou & Lei, 2025). Firms that prioritize transparency, accountability, and stakeholder interests are more likely to adopt prudent reporting practices that enhance the credibility of financial information (Mio et al., 2023). Such characteristics are consistent with the principles of accounting conservatism, which emphasize the timely recognition of losses and a cautious approach to recognizing gains (Krismiaji & Sururi, 2021).

Consistent with this argument, Dalcero et al. (2025) provide evidence that ESG performance positively affects accounting conservatism, suggesting that sustainability-oriented firms tend to adopt more conservative financial reporting policies. Accounting conservatism plays an important role in improving financial reporting quality and mitigating information asymmetry between managers and investors (Basu, 1997). Conservative reporting practices can limit managerial opportunism, increase the reliability of accounting information, and strengthen investor confidence in corporate disclosures (Chen et al., 2023). As investors increasingly rely on credible information when evaluating corporate prospects and risk exposure, accounting conservatism may contribute to lower perceived investment risk and improved financing conditions (Widiatmoko et al., 2023).

One important consequence of reduced information asymmetry is a lower cost of equity capital (Chen et al., 2023). The cost of equity capital represents the return required by investors for providing equity financing and serves as a key determinant of corporate financing decisions (Chen et al., 2023; Mio et al., 2023). To support business expansion and operational development, companies rely on both internal and external funding sources, including equity and debt financing (Muzian et al., 2023). In Indonesia, the average cost of equity capital reaches 11.6%, exceeding that of neighboring countries such as Malaysia and Singapore, where it ranges between 8% and 10% (Widowati et al., 2025). This indicates that Indonesian firms are still perceived as relatively high-risk, making financing efficiency an important issue. In addition to its influence on accounting conservatism, ESG performance may also affect the cost of equity capital. Chen et al. (2023) Evidence suggests that ESG performance is inversely related to the cost of equity capital, meaning that companies with stronger sustainability outcomes tend to benefit from lower financing costs.

Corporate governance mechanisms, particularly managerial ownership, are also recognized as important determinants of investor confidence (Widiatmoko & Indarti,2024).

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When managers hold ownership stakes in the company, their interests are more likely to converge with those of shareholders, which helps reduce agency conflicts and promotes a more prudent approach to financial reporting (Javaid et al., 2023). Furthermore, Christian et al. (2022) find that managerial ownership is positively associated with accounting conservatism, while Faysal et al. (2021) indicates that as managerial ownership increases, firms tend to experience a reduction in their cost of equity capital.

Firm specific financial characteristics such as profitability may also affect accounting behavior and investor perceptions (Widiatmoko & Indarti, 2024). More profitable firms tend to adopt more prudent reporting practices to maintain earnings credibility and stakeholder trust, leading to greater degrees of accounting conservatism. (Widaryanti, 2022). Consistent with this view, Halim (2021) finds a significant and positive association between a firm's profitability and its level of accounting conservatism. Moreover, firms with higher profitability are typically viewed as carrying lower risk and greater financial stability, which in turn lowers investors' expected returns and reduces the cost of equity capital (Ismail & Obiedallah, 2022). Supporting this argument, Widiatmoko & Indarti (2024) document a significant negative association between firm profitability and the cost of equity capital.

This study builds upon the work of Widiatmoko & Indarti (2024), who examined the impact of corporate governance and profitability on accounting conservatism and the cost of equity capital. However, ESG performance was not incorporated into their research model, despite growing evidence suggesting that sustainability related factors influence both financial reporting quality and financing costs. Consequently, limited evidence is available regarding the simultaneous the influence of ESG performance, managerial ownership, and profitability on accounting conservatism and the cost of equity capital, particularly in emerging market settings.

Accordingly, this study extends the model by Widiatmoko & Indarti (2024) by incorporating ESG performance, adopted from (Chen et al., 2023). In addition, this research employs a more recent observation period covering 2020–2024, thereby providing updated empirical findings on the impact of ESG performance, managerial ownership, and profitability on accounting conservatism and the cost of equity capital among manufacturing firms listed on the Indonesia Stock Exchange (IDX). The novelty of this study lies in integrating ESG performance into the association between governance mechanisms, financial performance, accounting conservatism, and the cost of equity capital within the Indonesian manufacturing sector.

Agency theory proposed by Jensen & Meckling (1976) describes the presence of conflicting interests between managers acting as agents and shareholders serving as principals. From this perspective, the relationship between corporate governance, accounting conservatism, and the cost of equity capital can be understood as part of efforts to reduce agency conflicts and information asymmetry. Effective governance mechanisms combined with prudent financial reporting may enhance transparency and reduce uncertainty, which in turn lowers the return required by investors and decreases the company’s cost of equity capital (Vitolla et al., 2020). Conversely, Stakeholder Theory Freeman (2015), emphasizes that firms bear responsibility not only toward shareholders but also to a wider array of stakeholders. Within this perspective, accounting conservatism can protect stakeholders from uncertainty by providing more reliable and verifiable financial information (Anagnostopoulou et al., 2021). Such reporting practices, supported by strong ESG performance, may enhance investor confidence, strengthen firm value, and ultimately reduce the cost of equity capital (Huang et al., 2022; Tampakoudis et al., 2023).

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As stakeholder expectations regarding corporate transparency continue to increase, firms are encouraged to provide more reliable and prudent financial reporting to reduce information asymmetry associated with ESG related risks (Schiehll & Kolahgar, 2021). Such prudence is reflected in the implementation of accounting conservatism, an accounting principle that emphasizes the timely recognition of potential losses over gains and contributes to higher quality financial reporting (Zadeh et al., 2022). In this context, firms with stronger ESG performance are more likely to adopt conservative accounting practices as a strategic mechanism to enhance the credibility of financial information and fulfill stakeholder expectations. This relationship suggests that sustainability-oriented firms not only demonstrate accountability through ESG disclosure but also strengthen reporting reliability through more prudent accounting practices. Empirical evidence from Anagnostopoulou et al. (2021), Burke et al. (2020), Dalcero et al. (2025), and Hong (2020) consistently supports a positive relationship between ESG performance and accounting conservatism. Drawing from these arguments, the following hypothesis is put forward:
Hypothesis 1: ESG performance has a positive effect on accounting conservatism

Managerial ownership denotes the percentage of shares owned by managers in relation to the total number of shares outstanding. When managers also act as shareholders, they are more likely to make decisions that are aligned with the company's long-term goals and aimed at maximizing shareholder value (Indarti et al., 2021). This dual role encourages managers to prioritize sustainable corporate performance while reducing possible divergence of interests between management and shareholders. As a result, managers have stronger incentives to maintain the credibility of financial reporting and to exercise greater prudence in accounting decisions. Such prudence is reflected in the adoption of accounting conservatism, which enables firms to recognize potential losses more cautiously and reduce the risk of overstating financial performance (Widaryanti, 2022). In this context, higher managerial ownership may encourage the implementation of more conservative accounting practices as a mechanism to protect firm value and minimize agency conflicts. Empirical evidence from companies listed in Spain and Portugal further supports this argument, indicating that higher levels of managerial ownership are associated with greater accounting conservatism (Indarti et al., 2021). Based on on the theoretical foundation and existing empirical evidence, the following hypothesis is advanced:
Hypothesis 2: Managerial ownership has a positive effect on accounting conservatism

As a key component of financial statements, profit provides relevant information for stakeholders and serves as an important indicator of management effectiveness. Consequently, investors and prospective investors frequently consider profitability when assessing a firm's financial performance and informing investment decisions (Widiatmoko & Indarti, 2024). Higher profitability may also encourage management to adopt more prudent accounting policies in order to reduce uncertainty, maintain reporting credibility, and strengthen stakeholder confidence in the company's financial condition (Ashari & Kusumawati, 2023). In this context, accounting conservatism functions as an important mechanism for ensuring that financial information is presented cautiously and reliably, particularly when profitability becomes a key basis for stakeholder evaluation (Widaryanti, 2022). Firms with stronger profitability may therefore be more likely to implement conservative accounting practices to preserve the quality of earnings and avoid overstating financial performance (Alkhafaji et al., 2020). Empirical evidence from Widiatmoko & Indarti (2024), Widaryanti (2022) and Widiatmoko et al. (2023), supports this argument by demonstrating that profitability is positively associated with accounting conservatism. Based

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on these theoretical arguments and existing empirical evidence, the following hypothesis is put forward:

Hypothesis 3: Profitability has a positive effect on accounting conservatism.

Strong ESG performance provide positive signals regarding sustainability, transparency, and effective risk management, which can strengthen investor confidence and enhance corporate credibility (Chen et al., 2023). Greater transparency through ESG disclosure may reduce information asymmetry between the company and investors while also lowering perceived investment risk (Tang, 2022). As a result, investors may require lower expected returns, which ultimately reduces the company's cost of equity (Murè et al., 2021). In this context, ESG performance serves as an important strategic mechanism for improving stakeholder trust and increasing access to more efficient financing. Empirical evidence from Chen et al. (2023) and Tang (2022) demonstrating that firms with stronger ESG performance tend to benefit from a reduced cost of equity. Building on these arguments, the following hypothesis is proposed:

Hypothesis 4: ESG performance has a negative effect on the cost of equity.

Managerial ownership can reduce this agency conflict by aligning management interests with shareholder interests, thereby encouraging managers to act more wisely and prioritize decisions that increase firm value (Jensen & Meckling, 1976). This alignment of interests can reduce agency costs, strengthen the effectiveness of internal oversight, and lower the level of risk perceived by investors. As investor perceptions of risk decline, the expected rate of return demanded by investors may also decrease, ultimately reducing the company's cost of equity capital (Faysal et al., 2020). Empirical evidence from Faysal et al. (2020) further supports this argument by demonstrating that managerial ownership has a negative influence on the cost of equity capital. Based on this reasoning, the following hypothesis is put forward:

Hypothesis 5: Managerial ownership has a negative effect on the cost of equity.

High profitability reflects a firm's capacity to generate earnings efficiently and may indicate lower business risk from the perspective of investors (Indarti et al., 2021). Strong financial performance can increase investor confidence by signaling that the company has greater capacity to sustain operations and generate future returns (Mardones & Cuneo, 2020). As a result, investors may require lower expected returns, which ultimately reduces the company's cost of equity capital (Zheng et al., 2021). Empirical evidence from Ismail & Obiedallah (2022) further supports this argument, demonstrating that firms with stronger financial performance tend to have a lower cost of equity capital. Based on these arguments, the following hypothesis is proposed:

Hypothesis 6: Profitability has a negative effect on the cost of equity.

Accounting conservatism can reduce information asymmetry between management and investors through more prudent financial reporting (Krismiaji & Astuti, 2021). By recognizing potential losses more cautiously, accounting conservatism may reduce investor uncertainty and strengthen the credibility of financial statements. This condition can lead investors to require lower expected returns, thereby reducing the cost of equity (Ashari & Kusumawati, 2023). In this context, accounting conservatism functions as an important mechanism for improving reporting quality and minimizing information asymmetry in capital markets. Research by Chouaibi & Belhouchet (2023) and Widiatmoko et al. (2023) demonstrating that accounting conservatism is negatively associated with the cost of equity capital. Based on these arguments, the following hypothesis is proposed:

Hypothesis 7: Accounting conservatism has a negative effect on the cost of equity

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The research model describing the relationship between variables in this study is depicted in Figure 1.

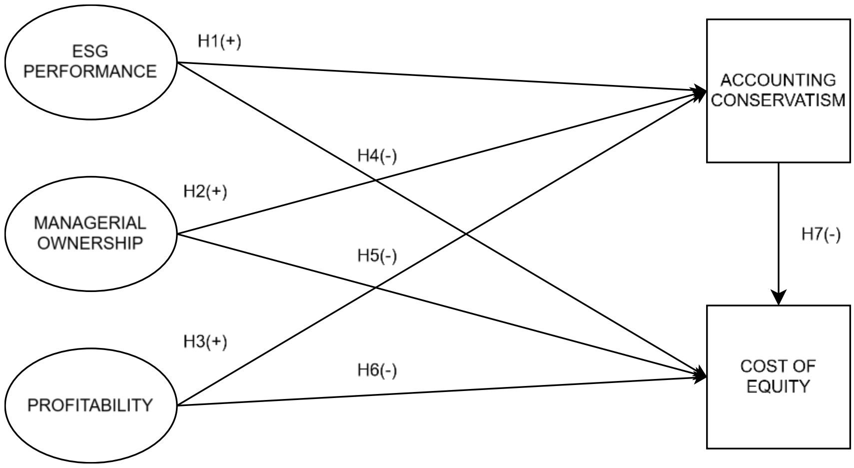

Figure 1. Research Model

2. METHODOLOGY

This research investigates manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the 2020–2024 period. The sample was determined through purposive sampling in accordance with the following criteria:

Table 1.Purposive Sampling

NO	Criteria	Sample
1.	Manufacturing firms listed on the IDX over the period 2020-2024	222
2.	Companies with available ESG scores from 2020–2024	22
3.	Potential firm-year observations (22 firms x 5 years)	110
4.	Less: Incomplete firm-year observations	(12)
5.	Final firm-year observations	98

This study uses cost of accounting conservatism (CONS) and Cost of equity capital (COE) and as the dependent variables. ESG performance, managerial ownership (MOS), and profitability (ROA) are included as the independent variables, while SIZE is incorporated as a control variable to control for its potential effect on the proposed relationships.

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Table 2. Variable Measurements

Variable	Measurements	References
COE	$r = \frac{(B_t + X_{t+1} - P_t)}{P_t}$ r :Cost of Equity Capital Bt :Book value per share it periode t X_{t+1} :Earnings per share in periode t+1 Pt :Stock price in periode t	Ohlson (2020)
CONS	$\left(\frac{Income\ before\ extraordinary + depreciation\ expense - net\ operating\ cashflow}{Total\ Assets}\right) x - 1$	Givoly and Hayn (2000)
ESG	Refinitiv ESG Score	Kusno et al. (2024)
MOS	$\frac{Number\ of\ shares\ owned\ by\ management}{Number\ of\ outstandings\ shares}$	Indarti et al. (2021)
ROA	$\frac{Earning\ after\ tax}{Total\ assets}$	(Widiatmoko & Indarti, 2024)
SIZE	Ln Total Assets	Widiatmoko et al. (2023)

Table 2 presents the operational definitions and measurement methods of all variables employed in this study. The cost of equity capital (COE) is estimated using the Ohlson (2020) model. Accounting conservatism (CONS) is measured using the accrual-based model proposed by Givoly and Hayn (2000). ESG performance is measured using the Refinitiv ESG Score following Kusno et al. (2024). Managerial ownership (MOS) is measured as the proportion of shares owned by management to the total outstanding shares following Indarti et al. (2021). Profitability is proxied by return on assets (ROA) following Widiatmoko and Indarti (2024), while firm size (SIZE) is measured using the natural logarithm of total assets following Widiatmoko et al. (2023). These measurement proxies were adopted from previous studies to ensure the validity and comparability of the empirical analysis.

This study applies two empirical models, namely Model 1 and Model 2. Model 1 is used to examine the effects of ESG performance, managerial ownership, and profitability on accounting conservatism. Model 2 is employed to analyze the effects of ESG performance, managerial ownership, profitability, and accounting conservatism on the cost of equity capital. The two research models are mathematically formulated as follows:

$$CONS = \beta_0 + \beta_1 ESG + \beta_2 MOS + B_3 ROA + \beta_4 SIZE + e \quad (1)$$

$$COE = \beta_0 + \beta_1 ESG + \beta_2 MOS + \beta_3 ROA + \beta_4 CONS + \beta_5 SIZE + e \quad (2)$$

3. RESULT AND DISCUSSION

Descriptive statistics for each variable used in this study are presented in Table 2. Prior to the main analysis, a box plot test was conducted to identify potential outliers in each research variable. Observations classified as outliers were subsequently winsorized at the 1% level to reduce the influence of extreme values while preserving the overall sample observations. This procedure was applied to ESG performance (ESG), cost of equity capital (COE), accounting conservatism (CONS), and profitability (ROA) by capping values at the lower and upper 1st

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percentiles. The winsorization procedure aimed to minimize the impact of extreme observations, improve data stability, and enhance the representativeness of the empirical results. Following this procedure, descriptive statistical analysis was carried out to summarize the data characteristics by presenting the minimum, maximum, mean, and standard deviation values for each variable.

Table 3. Descriptive Statistics

Variable	Obs	Means	Std.dev.	Min	Max
COE	98	-0.3145286	0.9408678	-0.9997126	4.590573
CONS	98	-0.0255078	0.0641374	-0.1522953	0.464771
ESG	98	50.22847	18.23187	14.71	82.75
MOS	98	0.0793102	0.2018234	0	0.7518
ROA	98	0.080742	0.726918	-0.0101255	0.3488514
SIZE	98	31.05708	1.746287	24.99157	33.78683

Source: data processed 2026

Based on the descriptive statistics in Table 3, all variables were measured using 98 observations. Accounting conservatism (CONS) recorded a mean value of −0.026 and a standard deviation of 0.064, indicating relatively low variation across the sample. The cost of equity capital (COE) showed a mean of −0.315 with a standard deviation of 0.941, reflecting a relatively high level of variation among observations. ESG performance reported an average value of 50.228 and a standard deviation of 18.232, suggesting substantial variation in sustainability performance across the sample firms. Managerial ownership (MOS) had a mean value of 0.079, indicating that the proportion of shares held by management was generally low. Profitability (ROA) recorded an average value of 0.081, suggesting that, on average, firms were able to generate positive earnings from their assets. Meanwhile, firm size (SIZE) reported a mean of 31.057 and a standard deviation of 1.746, indicating that the sample firms were relatively large with limited variation across observations.

Classical assumption tests were conducted, including tests for heteroscedasticity, autocorrelation, and multicollinearity, as well as model specification tests (Chow test and Hausman test) to determine the most appropriate estimation model among the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). Based on these test results, the Fixed Effect Model (FEM) was selected as the most suitable model. Furthermore, given the indication of autocorrelation issues, the model was estimated using FEM with cluster robust standard errors to produce more efficient and consistent estimation results.

Table 4 presents the regression results for Model 1, which examines the effects of ESG performance, managerial ownership, and profitability on accounting conservatism. The model is statistically significant (F-statistic = 3.55; p = 0.0176), indicating that the independent variables jointly explain variations in accounting conservatism. The adjusted R-square value of 0.4534 suggests that approximately 45.34% of the variation in accounting conservatism is explained by the variables included in the model.
Test Result of Model 1

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Table 4. Test Result of Model 1

Variable	Coefficients	T statistic	Prob	Conclusion
(Constant)	4.7754	2.62	0.016	
ESG	0.00138	2.11	0.047	H1 is supported
MOS	1.1633	1.75	0.095	H2 is not supported
ROA	-0.2728	-1.09	0.289	H3 is not supported
SIZE	-0.15314	-2.59	0.016	-
Adjusted R-Square		0.4534		
F-statistic		3.55		
Sig.		0.0176		

Source: data processed 2026

ESG Performance Impact on Accounting Conservatism

Based on Table 4, the results indicate that ESG performance has a positive and significant effect on accounting conservatism, with a beta coefficient of 0.00138 and a significance level of 0.047 (<0.05), thereby supporting the proposed hypothesis. This finding suggests that firms with stronger ESG performance are more likely to adopt conservative accounting practices in their financial reporting. The result is consistent with Stakeholder Theory, which argues that companies are encouraged to enhance transparency and improve the quality of financial information in order to meet stakeholder expectations. Effective ESG implementation increases stakeholder scrutiny and motivates management to adopt more prudent reporting practices as a means of reducing information asymmetry and maintaining corporate credibility (Manaf et al., 2024) . This finding also supports the view that firms with strong ESG commitments tend to strengthen the credibility of financial reporting through more cautious accounting policies. Furthermore, the result is consistent with Dalcero et al. (2025), ho found that ESG performance positively influences accounting conservatism through improvements in information quality and stronger corporate reputation among stakeholders.

Managerial Ownership Impact on Accounting Conservatism

Managerial ownership (MOS) has a beta coefficient of 1.1633 with a significance level of 0.095 (>0.05), indicating that managerial ownership does not have a significant effect on accounting conservatism. Therefore, the proposed hypothesis is not supported. This finding is inconsistent with Agency Theory proposed by Jensen & Meckling (1976), which suggests that managerial share ownership can align the interests of management and shareholders, thereby encouraging managers to make decisions that support long-term firm value, including the adoption of more conservative accounting practices. One possible explanation is that the average level of managerial ownership in manufacturing firms in Indonesia remains relatively low, and in some firms management does not hold any shares at all (Widiatmoko & Indarti,2024). This limited ownership may weaken management's sense of responsibility toward long-term firm performance and reduce the incentive to apply conservative accounting policies in financial reporting (Agustina et al., 2023). The result of this study is

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consistent with prior research by Agustina et al. (2023) and Widiatmoko & Indarti (2024), both of which found that managerial ownership does not significantly affect accounting conservatism. However, these findings contradict earlier studies by Alves (2020) and Indarti et al. (2021), which demonstrated that higher managerial ownership encourages management to adopt more conservative financial reporting practices due to stronger alignment between managerial and shareholder interests.

Profitability Impact on Accounting Conservatism

Profitability (ROA) has a beta coefficient of -0.27284 with a significance level of 0.289 (>0.05), indicating that profitability does not have a significant effect on accounting conservatism. Therefore, the proposed hypothesis is not supported. This finding suggests that the level of corporate profitability does not determine the extent to which firms apply accounting conservatism in financial reporting. The result is inconsistent with Agency Theory, which argues that firms with higher profitability are more likely to adopt conservative accounting practices to reduce agency conflicts and information asymmetry between management and shareholders. The insignificant relationship indicate that profitability does not serve as a direct determinant of accounting conservatism. Firms with lower profitability are not necessarily less conservative, as accounting policies are more strongly influenced by governance structures, accounting standards, and managerial discretion rather than short term financial performance (Ashari & Kusumawati, 2023). This finding is consistent with Dalcero et al. (2025), who reported that profitability does not have a consistent effect on accounting conservatism, indicating that profit performance does not necessarily reflect a company's level of prudence in financial reporting. However, this result differs from the findings of Widaryanti (2022) and Widiatmoko et al. (2023), which demonstrated that firms with higher profitability tend to implement greater accounting conservatism in order to maintain earnings quality and strengthen the credibility of financial statements.

Test Result of Model 2

Tabel 5.Test Result of Model 2

Variable	Coefficients	T statistic	Prob	Conclusion
(Constant)	2.1780	0.23	0.818	
ESG	0.0142	0.88	0.387	H1 is not supported
MOS	-7.7611	-3.55	0.002	H2 is supported
ROA	-1.0222	-0.49	0.628	H3 is not supported
CONS	0.2230	0.20	0.844	
SIZE	-0.0806	-0.25	0.818	-
Adjusted R-Square		0.1006		
F-statistic		3.79		
Sig.		0.0179		

Table 5 displays the regression output for Model 2, which assesses how ESG performance, managerial ownership, profitability, accounting conservatism, and firm size influence the cost

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of equity. The model achieves statistical significance (F-statistic = 3.79; p = 0.0179), confirming that the independent variables collectively account for variations in the cost of equity. With an adjusted R-square of 0.1006, the model explains roughly 10.06% of the variation observed in the cost of equity.

ESG Performance Impact on Cost of Equity

Based on the results presented in Table 5, ESG performance does not exert a significant influence on the cost of equity, as reflected by a significance level of 0.387 (>0.05). Therefore, the proposed hypothesis is not supported. This finding indicates that ESG information has not yet been fully incorporated into investors' pricing decisions in emerging markets, where investment valuation is still primarily driven by financial fundamentals such as return and risk indicators (Jafar et al., 2024; Nabila et al., 2024). Consequently, ESG performance does not appear to function as a strong risk signal in determining investors' required returns. Although Stakeholder Theory emphasizes that ESG disclosure enhances transparency and reduces perceived risk, this effect may not yet be fully reflected in market-based valuation processes in emerging economies. This result is consistent with Termprasertsakul et al. (2026), who found that ESG performance does not significantly affect the cost of equity capital. Their study also explained that investors do not consistently perceive ESG performance as an indicator capable of reducing investment risk or lowering the expected return on shares. In addition, the limited quality of ESG disclosures and the relatively weak integration of ESG considerations into investment decision-making may reduce the relevance of ESG information in influencing the cost of equity capital (Termprasertsakul et al., 2026).

Managerial Ownership Impact on Cost of Equity

The managerial ownership (MOS) variable has a beta coefficient of -7.761172 with a significance level of 0.020 (<0.05), indicating that managerial ownership has a significant negative effect on the cost of equity capital. Therefore, the proposed hypothesis is supported. This result indicates that a greater proportion of shares held by management tends to correspond with a reduced cost of equity capital. The result is in line with Agency Theory as articulated by Jensen & Meckling (1976), which posits that managerial ownership can mitigate agency problems by bringing the interests of managers and shareholders into closer alignment. When managers hold company shares, they are more likely to be motivated to maximize firm value and make decisions that reflect shareholders' interests. This alignment reduces agency conflicts and lowers information asymmetry, leading investors to perceive the company as having lower risk. As a result, investors may require a lower rate of return, thereby reducing the cost of equity capital. This finding is consistent with prior studies by Dakhlaoui & Gana (2020) and Rosa et al. (2020), which also reported that managerial ownership contributes to lower equity financing costs by increasing investor confidence and strengthening the effectiveness of corporate governance.

Profitability Impact on the Cost of Equity

Profitability (ROA) has a beta coefficient of -1.0222 with a significance level of 0.628 (>0.05), indicating that profitability does not have a significant effect on the cost of equity capital. Therefore, the proposed hypothesis stating that profitability has a negative effect on the cost of equity capital is not supported. This finding suggests that profitability is not a determining factor in investors' required rate of return within the observed firms. The result is inconsistent with Agency Theory, which suggests that highly profitable firms are expected to reduce information asymmetry and perceived investment risk, thereby lowering the cost

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of equity capital. However, profitability alone is insufficient to influence investors' required returns. As argued by Ismail & Obiedallah (2022), profitability is often already reflected in market expectations and stock prices, making it less relevant as an additional signal in determining the cost of equity capital. Consequently, firms with higher profitability do not necessarily experience lower equity financing costs if investors continue to perceive similar levels of risk. This finding is consistent with the studies of Silalahi et al.(2023) and Simanjuntak et al. (2025), which also reported that profitability does not significantly affect the cost of equity capital. These findings indicate that profitability is not a determining factor in the cost of equity capital among the sampled firms. This suggests that the level of profitability alone is insufficient to explain variations in investors' required returns.

Accounting Conservatism Impact on the Cost of Equity

Accounting conservatism (CONS) has a coefficient value of 0.22300 with a probability (p-value) of 0.844 (>0.05), indicating that accounting conservatism does not have a significant effect on the cost of equity. Therefore, the proposed hypothesis is not supported. This finding indicates that accounting conservatism is not a determining factor in investors' required rate of return among the sampled firms. The result is inconsistent with Agency Theory, which posits that accounting conservatism can reduce information asymmetry and agency conflicts, thereby lowering the cost of equity capital. Following IFRS convergence, conservatism has largely evolved into the concept of prudence, making prudent reporting practices an inherent part of financial reporting (Suwarno, 2025). As a result, differences in the level of accounting conservatism may no longer provide additional information that is relevant to investors in assessing firm risk and determining required returns. Furthermore, prior studies suggest that the effect of conservatism on the cost of equity tends to diminish when firms operate in relatively transparent information environments, where investors have access to alternative sources of information for evaluating firm risk and performance (Sari & Lastiati, 2025).This finding is consistent with Widiatmoko et al. (2023), who also found that accounting conservatism does not have a significant effect on the cost of equity capital. These findings indicate that investors evaluate not only the quality of financial reporting, but also the company's overall financial condition and risk profile when making investment decisions.

4. CONCLUSSION

This study investigates both the direct and indirect effects of ESG performance, managerial ownership, profitability, and accounting conservatism on the cost of equity. The results suggest that companies exhibiting higher ESG performance tend to adopt more conservative financial reporting practices, reflecting higher levels of transparency, accountability, and financial reporting quality. In contrast, managerial ownership and profitability do not have a significant effect on accounting conservatism. Furthermore, managerial ownership is found to reduce the cost of equity, whereas ESG performance, profitability, and accounting conservatism are not considered by investors as primary determinants in assessing the required rate of return on equity investments.

These findings provide several theoretical implications. First, the study supports Stakeholder Theory by demonstrating that firms with stronger ESG performance tend to strengthen transparency and accountability through more conservative financial reporting practices. Second, the negative relationship between managerial ownership and the cost of equity supports Agency Theory, suggesting that managerial share ownership serves to bring the interests of managers and shareholders into closer alignment, reduces agency conflicts,

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and lowers investors' perceived risk. Third, this study contributes to the growing debate on the economic consequences of ESG performance. While prior studies generally suggest that ESG initiatives reduce financing costs by enhancing transparency and reducing information asymmetry, the findings reveal that ESG performance improves accounting conservatism but does not directly reduce the cost of equity. This evidence suggests that the benefits of ESG performance may be reflected primarily in reporting quality rather than in immediate capital market outcomes, particularly within emerging market environments. In addition, the findings indicate that accounting conservatism is no longer perceived by investors as a dominant signal in evaluating firm risk and making investment decisions.

From a practical perspective, this study highlights the importance of ESG implementation in enhancing financial reporting quality and corporate credibility. The findings indicate that firms with stronger ESG performance tend to adopt more conservative reporting practices, suggesting that sustainability initiatives can improve transparency and accountability. However, ESG performance does not significantly reduce the cost of equity, implying that investors in emerging markets may not yet fully incorporate ESG information into their investment decisions. Therefore, companies should focus not only on improving ESG performance but also on enhancing the quality and credibility of sustainability disclosures. The role of accounting conservatism has evolved following the convergence of International Financial Reporting Standards (IFRS), which place greater emphasis on fair value measurement and information neutrality rather than conservative reporting principles. As explained by Suwarno (2025), conservatism is no longer explicitly recognized as a primary principle within the IFRS conceptual framework because it may introduce bias in financial reporting. However, accounting conservatism remains relevant in accounting research due to its association with financial reporting quality, information asymmetry, corporate governance, and agency related issues.

Although this study offers valuable contributions, it is subject to several limitations. The sample is restricted to manufacturing firms that consistently disclose ESG information, and given that relatively few Indonesian firms meet this criterion, the sample may not fully represent the broader population of manufacturing firms in Indonesia. Furthermore, the model's explanatory power indicates that factors beyond those examined in this study may also affect accounting conservatism and the cost of equity. Future research is therefore encouraged to include additional corporate governance variables, ownership structures, and board characteristics, and to broaden the industry scope and observation period to provide more comprehensive insights into the determinants of accounting conservatism and the cost of equity.

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