UNIVERSITI TEKNOLOGI MARA

THE EFFECT OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) DISCLOSURE AND SHARIAH-COMPLIANCE ON FIRM PERFORMANCE AMONG LISTED FIRMS IN MALAYSIA

NIK NUR FARAHIYAH BINTI NIK ASNI

Thesis submitted in fulfilment
of the requirements for the degree of
Master of Science
(Accountancy)

Faculty of Accountancy

September 2025

ABSTRACT

Public listed firms (PLFs) in Malaysia are increasingly expected to demonstrate responsible practices in response to environmental, social, and governance (ESG) challenges. These include environmental degradation, social inequality, and weak governance structures, all of which can significantly impact firm performance (FP). In the meantime, the growing emphasis on Shariah-compliance, which is guided by Islamic principles of ethical conduct, fairness, and social responsibility, raises questions on how Shariah-compliance status (SCS) interacts with ESG disclosure in influencing firm performance. This study examines the effect of ESG disclosure and Shariah-compliance status (SCS) on the firm performance of Malaysian PLFs from 2020 to 2023. This study also examines whether SCS moderates the ESG-performance relationship. Using pooled data analysis with industry and year effects, the study analyses 798 firm-year observations, with firm performance measured by Tobin's Q, return on assets (ROA), return on equity (ROE), and cash holdings (CH). ESG scores and financial data were retrieved from Refinitiv DataStream, while SCS classification was sourced from the Securities Commission Malaysia. This study addresses the limited research examining the combined effect of ESG disclosure and Shariah-compliance status (SCS) on firm performance, particularly within the Malaysian context. The findings reveal that ESG disclosure positively influences firm performance, with social disclosure consistently showing the strongest impact, underscoring the operational and financial value of stakeholder-oriented initiatives. The study further finds that while SCS enhances market-based performance (Tobin's Q), it is associated with lower accounting-based performance (ROA and CH), suggesting a trade-off rooted in conservative financial practices under Islamic principles. Importantly, the moderating role of SCS strengthens the positive relationship between social, governance, and ESG controversies disclosures and firm performance, but not environmental disclosure, highlighting that the ethical and reputational aspects of Shariah compliance align more closely with certain ESG dimensions. These results extend prior research by empirically demonstrating that Shariah compliance reinforces selected ESG components, addressing the research gap on how dual screening mechanisms (ESG and SCS) interact to influence firm performance. Grounded in stakeholder and legitimacy theories, this study contributes to understanding how ESG and Islamic principles jointly shape firm outcomes in a Muslim-majority capital market. It also offers insights for firms, investors, and policymakers aiming to integrate ethical, sustainable, and financial goals in support of Malaysia's Thirteenth Plan.

ACKNOWLEDGEMENT

Firstly, I wish to thank Allah the Almighty for giving me the opportunity, ability and strength to embark on my Master's and complete this thesis. My gratitude and thanks go to my beloved supervisor, Associate Professor Dr. Raja Adzrin Raja Ahmad, and my co-supervisor, Dr. Nurul Azlin Azmi. I truly appreciate their help, inspiration, time, input, advice, guidance, and unwavering support. My appreciation goes to the Postgraduate Studies Center (PPS) of the UiTM Johor Branch for their guidance and support in ensuring that I am on track for the study.

My deepest appreciation and heartfelt thanks go to my beloved husband, Mr. Amin Safwan Adnan, for his unwavering love, support, encouragement, and understanding. He has been my greatest source of strength and my number-one supporter throughout my journey toward further studies.

I am also profoundly grateful to my family and in-laws, especially my parents, Mr. Nik Asni Nik Cob and for their endless du'a, guidance, and encouragement in shaping every step of my life. My heartfelt thanks also extend to my wonderful siblings—Nik Muhammad Aizuddin, Nik Muhammad Azim, Nik Muhammad Awis, and Nik Nur Faiqah—who fill my life with endless joy, laughter, and cherished moments.

Thank you for all your unwavering support.

TABLE OF CONTENTS

CHAPTER 1
INTRODUCTION

1.1 Chapter Overview

This chapter provides an overview of the study. Section 1.2 discusses the research background, while Section 1.3 outlines the problem statement related to ESG issues and Shariah-compliance globally and in Malaysia. Section 1.4 presents the research questions, and Section 1.5 states the objectives. Sections 1.6 to 1.8 cover the study's scope, significance, and operational definitions. Finally, Section 1.9 summarises the thesis structure.

1.2 Research Background

Firm performance has long been a central concern among policymakers, researchers, and business leaders, as it directly influences economic stability, employment, and national growth (Rehman et al., 2014). In Malaysia, sustaining strong performance has become increasingly challenging due to economic uncertainty, rising global competition, human resource issues, and technological gaps (Malaysian Investment Development Authority, 2024; Sapiai et al., 2024). Additionally, corporate scandals and governance failures have highlighted weaknesses in operational efficiency and accountability, potentially undermining investor confidence and long-term performance (Bhatt & Bhatt, 2017; Ghazali, 2020). With Malaysia's aspiration to become a high-income nation under the Thirteenth Malaysia Plan (RMK-13), improving firm performance is essential to support broader economic goals.

To address the challenges of maintaining firm performance, there is a growing emphasis on non-financial business dimensions, particularly environmental, social, and governance (ESG) practices. Increasing public criticism of environmental harm and social injustice has pushed firms to become more transparent and accountable (Whetman, 2017), as poor ESG performance can damage reputation, invite boycotts, and ultimately harm financial returns and shareholder value. While investors once focused mainly on financial outcomes, they are now increasingly concerned about how profits are achieved (Aydogmus et al., 2022). According to the PwC 2021 Global