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# Evaluating the Impact of Sustainability Reporting on Financial Performance: The Mediating Role of ESG Performance and the Moderating Role of Firm Size

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**Abstract**
As sustainability assumes a more prominent position in corporate strategic planning, this research investigates the influence of sustainability reporting on the financial outcomes of companies listed on the Pakistan Stock Exchange, considering environmental, social, and governance performance and firm size as explanatory factors. With the increased international focus on ESG disclosures, the study fulfills the lack of empirical research in developing economies, such as Pakistan. The research design is a quantitative one, as primary data will be collected using a structured questionnaire that is closed-ended and will be administered to 400 employees working in different sectors in Pakistan. They were investigated in four dimensions: sustainability reporting, ESG performance, financial performance, and firm size. The SPSS was applied to conduct data analysis, including descriptive statistics, correlation, and reliability tests, as well as mediation and moderation regression models. Instructed by the resource-based view and the stakeholder theory, the study highlights the importance of strong ESG strategies in creating a competitive advantage over time and increasing financial performance. The evidence indicates that there is a positive association between the overall sustainability reporting and financial performance that is conditioned by the size of firms and mediated by ESG performance. The research has some practical implications for the business, encouraging them to adopt harmonized ESG disclosure standards, and capacity-building efforts should be offered to smaller companies to enhance their integration of sustainability. Policy-wise, the study requires policy measures in the form of regulations that would help in achieving uniformity in ESG practices among companies. Cross-sectional data nature and using self-reported responses as the data are the limitations, as they can present a bias of response. Altogether, the current research contributes to the scholarly discussion and provides practical conclusions about the development of sustainable business in emerging economies.
**Keywords:** Sustainability Reporting, ESG Performance, Financial Performance, Firm Size

## 1. Introduction

In recent years, organizations globally have increasingly embraced sustainability, prompted by rising awareness of environmental issues, social responsibility, and matters of governance. Businesses are now expected not only to generate profits but also to communicate their sustainability initiatives transparently. Sustainability reporting has become a widely adopted mechanism for highlighting non-financial achievements in domains such as the environment, society, and corporate governance. Such reporting is recognized as a means of strengthening company reputation, fostering stakeholder trust, and contributing positively to overall financial standing. Organizations operating internationally now consider sustainability metrics reporting to be a fundamental aspect of business conduct, reflecting a significant shift from when it was a voluntary practice (Kassinis et al., 2022; Kuo et al., 2022; Audi et al., 2025). The increased attention to sustainability reporting is largely due to the recognition that future business success is tied to achieving sustainable development goals and addressing stakeholder interests (Al-Najjar & Abed, 2021; Mahmood et al., 2018; Sulehri & Ali, 2024; Sadiq et al., 2025).

The returns on sustainability reporting may be materialized in the form of improvements in transparency in reporting the environmental impact of the company along with the social responsibility activities and governance mechanisms. Important frameworks that guide and standardize corporate sustainability reports include the Global Reporting Initiative, the Sustainability Accounting Standards Board, and the International Integrated Reporting Council. These guidelines help stakeholders evaluate an organization's genuine commitment to sustainability practices (Mansour et al., 2023; Maroun, 2020; Sulehri et al., 2024). The data disclosed in such reports enables investors, regulators, and consumer advocacy groups to make more informed decisions. Consequently, sustainability reporting is now seen as a critical factor that influences the profitability of organizations. There is a robust body of scholarly work exploring the link between sustainability reporting and organizational financial performance. Several studies suggest that the disclosure of sustainability practices can enhance financial outcomes by improving reputation, mitigating risks, attracting investment, and broadening stakeholder engagement (Eccles et al., 2014; Malik, 2015; Audi et al., 2025). Conversely, some researchers argue that the costs associated with adopting sustainability practices may exceed the benefits for smaller organizations (Audi et al., 2024; Nguyen et al., 2022; Aggarwal, 2013). Such trade-offs could be more intensive in the case of developing nations such as Pakistan because the lack of financial and technical resources limits the potential of SMEs to adopt and report on sustainability initiatives. However, the consensus in the literature is that transparency regarding sustainability efforts tends to yield positive financial results in the long term, driven by more efficient operations, reduced environmental harm, and greater access to sustainable funding sources (Roussel & Audi, 2024; García-Sánchez et al., 2023; Khan & Hassan, 2019; Fatemi et al., 2018). Therefore, a nuanced understanding of the effects of sustainability reporting on financial outcomes is crucial, especially considering the mediating and moderating influences present.

Environmental, Social, and Governance (ESG) performance provides a practical link between sustainability disclosures and the financial outcomes of organizations. While sustainability reports articulate the intentions (Al-Najjar & Abed, 2021; Mahmood et al., 2018; Sulehri & Ali, 2024; Sadiq et al., 2025). strategies of companies, performance in environmental, social, and governance areas reflect the actual outcomes of these initiatives. High environmental, social, and governance scores can make disclosures more credible and reinforce stakeholder confidence (Zhou et al., 2024; Farhadi & Zhao, 2024; Hussain et al., 2018). For example, if an organization extensively reports on sustainability but performs poorly in evaluations of environmental, social, and governance

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factors, stakeholders may doubt the authenticity of its disclosures. Thus, actual performance in environmental, social, and governance domains bridges the gap between sustainability communication and the resultant financial consequences, influencing organizational value and profitability (Friede et al., 2015; Al Masri & Wimanda, 2024).

Firm size is an important moderating variable in the relationship between sustainability reporting and financial performance. Larger organizations, possessing more resources, heightened public visibility, and greater regulatory scrutiny, are generally better positioned to implement and communicate comprehensive sustainability strategies (Ahmed & Alvi, 2024; Zheka & Vishnevsky, 2022; Agyemang-Mintah et al., 2021; Plumlee et al., 2015). This difference by size is especially applicable in the Pakistani context where large companies experience higher expectations by investors and regulatory scrutiny whereas small companies tend to lack formal ESG frameworks. The effect of sustainability reporting on financial performance is thus shaped by organizational size, offering practical guidance for both policymakers and business leaders aiming to promote sustainable business practices (Dai et al., 2023; James & Emons, 2023). The growing demand for environmental, social, and governance-related information from investors and stakeholders has amplified the significance of research in this area. Asset managers and institutional investors are increasingly factoring in environmental, social, and governance data when making investment choices, seeking clear and credible sustainability disclosures from companies (Edward, 2022; Friede & Busch, 2022; Krüger, 2015). Organizations that provide detailed accounts of their sustainability initiatives typically benefit from lower costs of capital and greater opportunities to attract ethically motivated investors. Consequently, poor performance in sustainability reporting can hinder a firm's competitiveness in capital markets, while robust reporting practices are likely to enhance reputation and profitability. Overall, transparent sustainability reporting plays a pivotal role in determining both the competitive standing and financial health of organizations.

From a theoretical perspective, the stakeholder theory and the resource-based view provide valuable frameworks for analyzing the connection between sustainability reporting and financial performance. According to stakeholder theory, long-term business success depends on addressing the interests of a wide array of stakeholders beyond just shareholders (Freeman et al., 2021; Donaldson & Preston, 1995). Sustainability reporting demonstrates an organization's accountability to employees, communities, customers, and governmental bodies. The resource-based view, on the other hand, suggests that environmental, social, and governance capabilities and reporting infrastructures represent strategic resources that are difficult for competitors to imitate and can lead to superior financial performance (Marc & Yu, 2024; Barney & Mackey, 2020; Hart, 1995). These perspectives facilitate a comprehensive understanding of the mechanisms through which sustainability disclosures affect financial outcomes.

Recent regulatory reforms and global sustainability initiatives further highlight the importance of rigorous sustainability reporting. Legislation such as the Corporate Sustainability Reporting Directive and international agreements like the Sustainable Development Goals have prompted organizations to adopt higher and more uniform standards for sustainability reporting (European Commission, 2023; Hahn & Kühnen, 2013). These developments have established sustainability concerns as equally important as financial reporting and have led companies to make their disclosures more thorough to comply with new regulations and address stakeholder expectations (Fadzil, 2021; Mahmood et al., 2022; Huseyin, 2023; Musa, 2024). As an example, the Securities and Exchange Commission of Pakistan (SECP) has recently issued ESG guidelines focused on improving the quality of disclosure and its compatibility with international standards. The convergence of regulatory requirements and stakeholder demands is compelling organizations to prioritize transparent and comprehensive sustainability reporting. Despite the growing focus on sustainability reporting, its direct effects on financial performance remain ambiguous in certain contexts, such as Pakistan. This uncertainty stems from the complexity of factors influencing the relationship between sustainability initiatives and profitability. Although sustainability reporting is intended to improve communication and foster broader stakeholder involvement, it does not guarantee enhanced financial performance. The effectiveness and quality of sustainability efforts, organizational size, and structural characteristics all mediate the extent of financial benefits derived from sustainability initiatives (Ullah & Sohail, 2020; Mirakhor, 2021; Turan, 2023; Javed et al., 2023; Ngo, 2023). In countries where regulatory and business practices are still evolving, such as Pakistan, empirical research is essential for informing the development of effective sustainability strategies.

## 2. Literature Review

The growing demand for transparency in business operations has driven organizations worldwide to adopt comprehensive sustainability reporting frameworks. These frameworks, especially those consistent with the principles of environmental, social, and governance practices, have become essential elements of corporate strategy, seeking to integrate economic performance with responsibilities toward society and the environment (Xie et al., 2020; Sustainability Accounting Standards Board, 2020; Das, 2024). On the Pakistani scene, the Securities and Exchange Commission of Pakistan (SECP) has already presented guidelines that comply with international frameworks, including the Global Reporting Initiative (GRI) and the Sustainability Accounting Standards Board (SASB), and are therefore especially applicable to Pakistani firms looking to enhance sustainability reporting (SECP, 2023). Substantial academic literature supports the existence of a relationship between high-quality sustainability disclosures and positive financial outcomes for companies, highlighting that transparent reporting can foster trust, improve stakeholder relationships, and ultimately enhance financial results (Chouaibi et al., 2022; Omri, 2022; Velte, 2022; Munir et al., 2024). Furthermore, research increasingly identifies environmental, social, and governance performance as a key mediating factor in this relationship, with firm size emerging as a significant contextual factor influencing the strength and direction of these effects (Rosli et al., 2024; Xiong, 2024; Namadi, 2023; García-Sánchez et al., 2023; Karhan, 2019). The present literature review draws upon both empirical and conceptual studies published from 2020 to 2025 to examine how sustainability reporting impacts financial performance, focusing particularly on the mediating role of environmental, social, and governance performance and the moderating influence of organizational size.

### 2.1. Sustainability Reporting and Financial Performance

Sustainability reporting has become an essential corporate practice in response to increasing stakeholder expectations for transparency and responsible governance. Numerous studies have established that sustainability reporting is positively associated with financial performance. For example, Xie and colleagues (2020) examined listed firms in Pakistan and concluded that comprehensive sustainability disclosures are linked with improved return on assets and return on equity, suggesting that increased transparency regarding environmental and social matters can enhance both profitability and firm valuation. In a related study, Agyemang-Mintah and colleagues (2024) analyzed Chinese energy companies and found that robust sustainability communication boosted investor confidence and firm valuation, particularly in international contexts such as those shaped by the Belt and Road Initiative. Nonetheless, not every disclosure indicates substantive improvements. As a risk, Salem et al. (2024) single out symbolic disclosure the reporting nominally focused on image-building but was designed to bring an operational change mainly in perpetually pressured firms. The ones mentioned below are recent: a South Asian textile firm that issued glossy sustainability reports but was fined due to labor rights violations presented an instance of a disclosure-practice gap (Business & Human Rights Resource Centre, 2024). Additionally, inconsistencies in environmental, social, and governance rating systems, as noted by Capelle-Blancard and Petit (2019), may create confusion for investors and constrain the real impact of these disclosures on financial outcomes. It is therefore crucial to differentiate between the form and substance of sustainability disclosures when assessing their effects on financial performance. The rationale underlying this relationship is informed by theoretical frameworks such as stakeholder theory. According to this perspective, organizations that account for the interests of a broad range of stakeholders—including shareholders, employees, customers, and communities—can legitimize their operations, build long-term trust, and ultimately achieve sustainable financial success (Xie et al., 2020; Hun et al., 2024). Institutional theory further supports this viewpoint by proposing that organizations adopt sustainability reporting practices to comply with evolving norms and regulatory expectations, thereby securing legitimacy and competitive advantage in their industries (Kilyachkov & Chaldaeya, 2021; Hahn & Ince, 2022).

### 2.2. Mediating Role of ESG Performance

The performance of environmental, social, and governance factors acts as a critical mediating mechanism in translating sustainability reporting into improved financial performance. Environmental, social, and governance performance measures the substantive outcomes of sustainability initiatives outlined in corporate reports. In a comparative analysis, Chouaibi and colleagues (2022) demonstrated that organizations excelling in environmental, social, and governance factors, especially in areas such as environmental innovation, consistently outperformed their peers financially, suggesting that tangible environmental, social, and governance achievements are the pathway through which sustainability disclosures impact financial metrics. Several studies further reiterate that robust strategies focused on environmental, social, and governance factors can mitigate organizational risk, attract long-term investors, and enhance operational efficiency (Friede et al., 2015; Osei & Acheampong, 2021; Velte, 2022). Digital technologies are ESG monitoring trends. As an illustration, Cui (2025) writes about the fact that generative AI aids in the real-time monitoring of ESG. Nevertheless, the described technologies are problematic in a developing market such as Pakistan, where they are expensive, digitalization infrastructure is lacking, and there are not enough qualified analysts to process ESG data. In the banking sector, meaningful engagement in environmental, social, and governance initiatives including reduction of environmental impact and increased community involvement has been linked with improved profitability (Salem et al., 2024; Fateh & Poulin, 2025). Active participation in environmental, social, and governance activities transforms visionary sustainability narratives into concrete, value-generating actions. The mediating influence of environmental, social, and governance performance also supports the broader notion of value creation that extends beyond mere regulatory compliance. Companies that integrate environmental, social, and governance principles into their core strategy benefit not only from higher employee morale but also from enhanced brand reputation and greater organizational agility, leading to stronger financial outcomes. When comprehensive environmental, social, and governance reporting is aligned with authentic performance, it becomes a powerful driver of sustainable and profitable business growth.

### 2.3. Moderating Role of Firm Size

Firm size is a significant moderating factor in the relationship between financial performance and sustainability reporting. Larger organizations typically possess greater resources, stronger infrastructure, and heightened visibility among stakeholders, which enhances their ability to implement and communicate sustainability initiatives effectively. Rosli and colleagues (2024) found that audit quality, used as a proxy for governance strength, amplified the link between sustainability reporting and financial performance for large firms. These organizations demonstrated superior internal controls and a higher tendency to apply standardized reporting practices, resulting in better environmental, social, and governance outcomes and greater financial gains. Additionally, prominent corporations are subject to increased reputational risk and greater scrutiny from investors, regulators, and civil society, which compels them to pursue substantive sustainability strategies rather than merely symbolic actions. This dynamic results in more comprehensive environmental, social, and governance implementation, yielding a stronger financial impact, as confirmed by Agyemang-Mintah and colleagues (2024), who reported that larger companies experience a more pronounced positive effect from sustainability disclosures compared to their smaller counterparts.

Smaller companies in Pakistan, however, have the following barriers to reporting: lack of technical expertise, ESG consultants access, and budget requirements. SECP and GRI have taken action by providing an easier sustainability framework and training programs specific to SMEs, that are expected to boost engagement in ESG disclosure (SECP, 2023). This move toward the democratization of reporting standards may eventually create a more level playing field, although large firms currently maintain a significant advantage in converting sustainability efforts into financial returns. Another important determinant of the link between sustainability reporting and financial performance is the degree of standardization in reporting practices. Fragmentation across environmental, social, and governance frameworks has led to inconsistent data reporting across organizations and sectors. The establishment of the International Sustainability Standards Board in 2022 represents a major step toward harmonizing global reporting standards, thereby improving the comparability and credibility of sustainability disclosures and increasing their relevance for investors and analysts (Financial Times, 2024).

Empirical research has shown that organizations adhering to globally recognized frameworks, such as those promoted by the Global Reporting Initiative, the Sustainability Accounting Standards Board, and the Task Force on Climate-related Financial Disclosures, are more likely to achieve superior environmental, social, and governance performance and financial success (Rosli et al., 2024). This boosts stakeholder trust in the credibility of disclosed information and contributes to a reduction in the cost of capital for organizations. Integrating standardized environmental, social, and governance disclosures into annual financial statements further institutionalizes sustainability within corporate operations, increasing transparency and strategic alignment. The process of collecting, reporting, and utilizing environmental, social, and governance data is being transformed by digital technologies. Advanced analytics, artificial intelligence, and blockchain are enhancing the reliability and timeliness of sustainability disclosures. Cui (2025) demonstrated that AI tools can automate ESG analytics, while blockchain ensures data integrity though access to such tools remains limited to larger, tech-savvy firms.

Blockchain technology, with its immutable and transparent data structures, can significantly enhance the verifiability of environmental, social, and governance metrics. The adoption of such innovations makes it possible for organizations to maintain trustworthy sustainability records, reducing the risk of misleading claims and increasing investor confidence. However, these technological advances are more accessible to larger firms, further reinforcing the moderating impact of firm size on the relationship between sustainability reporting and financial performance. The influence of sustainability reporting on financial outcomes also varies by industry. Sectors with high environmental or social impact such as energy, finance, and manufacturing derive more substantial economic value from sustainability initiatives, given the regulatory pressures and stakeholder expectations they face. Agyemang-Mintah and colleagues (2024) observed that energy-intensive firms attracted greater investor attention when they issued detailed sustainability disclosures. Conversely, firms in lower-impact industries may not realize significant financial benefits from sustainability reporting unless it is integrated into a broader strategic initiative. Thus, industry-specific factors such as regulatory frameworks and stakeholder pressure further moderate the relationship between sustainability reporting and financial performance. Overall, the literature reveals a positive but complex association between sustainability disclosures and financial outcomes, with environmental, social, and governance performance serving as a central mediating mechanism and firm size shaping the strength of the relationship. Larger organizations, owing to their resource advantages and stakeholder prominence, are better positioned to capitalize on sustainability activities. At the same time, the standardization of reporting frameworks and the rise of digital technology increase the reliability and economic value of environmental, social, and governance practices. Nonetheless, challenges such as symbolic reporting, rating discrepancies, and unequal access to reporting infrastructure remain. Future research should prioritize longitudinal designs, sector-specific investigations, and technological innovation in the management of environmental, social, and governance data to further clarify this complex relationship.

## 3. Theoretical Framework

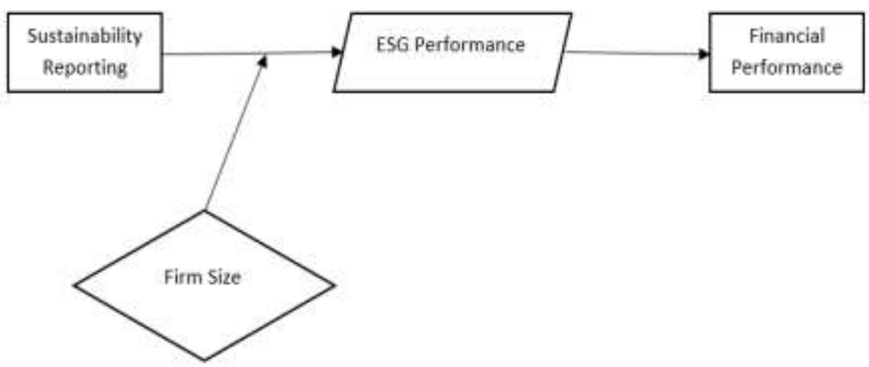


**Figure 1: Theoretical Framework (Freeman, 1984)**

Freeman (1984) introduced the Stakeholder Theory to point out that all stakeholders, and not only shareholders, should be considered in making business decisions. The Global Reporting Initiative aligns with this principle by promoting sustainability reporting, which encourages companies to disclose their environmental, social, and governance activities to a broad range of stakeholders. Organizations engaged in sustainability reporting seek to meet their obligations to communities, regulators, employees, customers, and investors. Clear and comprehensive sustainability reporting is widely found to build stakeholder trust, enhance corporate reputation, and strengthen financial resilience (De Villiers et al., 2021). Research by Akbar et al. (2022) and Gerged et al. (2021) further demonstrates that companies prioritizing sustainability reporting tend to experience reduced risk exposure and improved long-term financial performance (Kraus et al., 2020; Qiu et al., 2021). Thus, Stakeholder Theory provides a compelling justification for studying the impact of sustainability disclosures on firm outcomes amid heightened stakeholder demands for responsible and sustainable business conduct (Font et al., 2022; Melloni et al., 2023). Furthermore, the positive relationship between sustainability reporting and financial performance can also be explained by how strong environmental, social, and governance practices are embedded in organizational operations, consistent with Stakeholder Theory. Organizations with robust environmental, social, and governance performance are often seen as well-managed and committed to the welfare of all stakeholder groups, thereby securing sustainable growth (Velte, 2022; Arvidsson & Dumay, 2021). High environmental, social, and governance ratings in sustainability reports signal alignment with stakeholder interests, translating into superior financial results (Bae et al., 2023; Rahman et al., 2022; Albitar et al., 2020). Such performance is recognized by stakeholders through enhanced customer loyalty, increased investor confidence, and greater employee engagement, all of which contribute to the financial benefits of non-financial reporting (Gangi et al., 2021; Giannarakis et al., 2023). In this way, environmental, social, and governance performance operationalizes the mechanisms by which Stakeholder Theory enables financial gains from stakeholder-centric business practices.

Firm size is another important dimension within stakeholder theory. Larger organizations typically face a more diverse and visible stakeholder base and are thus subject to higher expectations for transparency and accountability (Amacha & Dastane, 2021; Yu & Luu, 2021). These companies generally have greater capacity to invest in sustainability initiatives and environmental, social, and governance programs, partly due to their heightened reputational risk if they fail to meet stakeholder expectations. As a result, large organizations are often more responsive to stakeholder concerns, and sustainability reporting tends to be more financially advantageous for them (Ali et al., 2023; Gerged, 2022). By contrast, smaller firms may not experience the same degree of stakeholder pressure and often lack the resources to implement comprehensive stakeholder-focused strategies. Studies confirm that larger firms tend to realize a stronger link between sustainability initiatives and financial outcomes due to their broader stakeholder engagement and resource availability (Birindelli et al., 2022; Michelon et al., 2020; Akisik & Gal, 2021). This ongoing relationship between organizational size and sustainability underscores how Stakeholder Theory explains the influence of different stakeholder groups on corporate performance and sustainability practices.

## 4. Methodology

This section outlines the methodological framework adopted in the present study, encompassing research design, target population and sample selection, data collection methods, instrument development, variable measurement, analytical techniques, and ethical considerations. The aim is to ensure the study's rigor, validity, replicability, and the provision of credible findings regarding the relationship between sustainability reporting and firm financial performance, with environmental, social, and governance performance as a mediator and firm size as a moderator.

### 4.1. Research Design

A quantitative research design underpins this study to analyze the extent to which firm financial performance is influenced by sustainability reporting, considering the mediating effect of environmental, social, and governance performance and the moderating influence of firm size. This approach allows for hypothesis testing, generalizability, and the assessment of statistical relationships among variables. The research adopts a positivist paradigm, presuming an objective reality that can be measured and analyzed statistically. The research encompasses the statistics between the years 2020 and 2024, which reveal the current tendencies of ESG reporting and financial statements in Pakistan. The study is explanatory in nature, aiming to determine causal relationships among the central constructs. This methodological approach aligns with contemporary research examining the impact of environmental, social, and governance factors and sustainability disclosures on financial performance through structured statistical models and secondary data (Faria et al., 2024; Kilic et al., 2022). The data collection tool was an ordered questionnaire that was designed concerning the previous scales that had been validated in peer-reviewed sources of literature. The main constructs, which include sustainability reporting, ESG performance, and financial outcomes, were borrowed from the works by Faria et al. (2024) and Khan et al. (2023). The questionnaires were given a pilot test to 25 respondents belonging to the target population to facilitate wording refinements, reliability checking as well as clarity before rolling them out fully.

### 4.2. Target Population and Sampling Technique

The target population comprises publicly listed non-financial companies on the Pakistan Stock Exchange. Non-financial firms are chosen because of their varied disclosure requirements and diverse approaches to establishing sustainability practices in industrial and commercial sectors. To ensure diversity and representativeness, a stratified random sampling method is used, with firms stratified by industry sectors such as textiles, cement, energy, and manufacturing. Within each stratum, random sampling is conducted to secure an unbiased selection of participants. The survey was conducted among mid-senior level managerial employees including sustainability officers, finance managers, and compliance heads. A response rate of 72.4 percent was attained which is satisfactory in statistical analysis.

### 4.3. Analytical Techniques

The data analysis methodology employs IBM SPSS, which offers a comprehensive range of statistical tools commonly used in business and behavioral research. The analytical process is structured to examine hypothesized relationships among sustainability reporting, environmental, social, and governance performance, firm size, and financial performance. An analysis is conducted in sequential stages to maximize the rigor and reliability of the study's findings.

### 4.4. Preliminary Data Screening

Before hypothesis testing, the dataset undergoes quality and statistical checks:

- Frequency tables and the Expectation-Maximization technique are utilized to address missing responses, with cases missing more than 10 percent of data excluded following Tabachnick and Fidell (2021).
- Outliers are identified using boxplots and the Mahalanobis distance, following guidelines from Hair et al. (2021).
- Skewness and kurtosis values are inspected, with values within ±2 deemed acceptable, as recommended by George and Mallery (2020). Visual inspection through histograms and Q-Q plots further informs normality assessment.

### 4.5. Reliability Analysis

Reliability refers to the internal consistency of measurement scales. For each construct, Cronbach's Alpha is computed to evaluate scale reliability, with a threshold of 0.70 considered adequate (Nunnally & Bernstein, 1994). Item-total correlations below 0.30 lead to item removal to enhance reliability. The key constructs measured include sustainability reporting, environmental, social, and governance performance, firm size, and financial performance.

This comprehensive methodology combines validated measurement scales, robust sampling, and advanced statistical analysis to explore the effect of sustainability reporting on firm financial performance in the context of emerging markets. The use of recent constructs and tools, grounded in literature from 2020 to 2025, contributes to the evolving scholarly conversation on environmental, social, and governance practices and sustainable finance.

### 4.6. Ethical Consideration

The ethical approval was provided by the Institutional Review Board (IRB) of the Lahore School of Accountancy and Finance. Respondents were informed and their consent was sought in participating in this study where participation was voluntary. The anonymity and confidentiality of data were preserved in the course of the research.

## 5. Results & Discussions

The primary focus of this study is the relationship between sustainability reporting and firm financial performance, considering environmental, social, and governance performance and firm size as moderating factors. Data were analyzed from four hundred responses using SPSS. The findings reveal statistically significant associations, underscoring the strategic importance of adopting sustainability initiatives to improve firm financial performance.

**Table 1: Descriptive Statistics and Reliability**

| Variable | Mean | SD | Cronbach's α |
|---|---|---|---|
| Sustainability Reporting (SR) | 3.84 | 0.71 | 0.89 |
| ESG Performance (ESG) | 3.76 | 0.68 | 0.91 |
| Financial Performance (FP) | 3.92 | 0.75 | 0.88 |
| Firm Size (FS) | 2.43 | 1.12 | – |

Table 1 presents the descriptive statistics and reliability analysis for the variables utilized in the present study. The average scores for the measured constructs indicate that respondents generally affirmed the survey items used to assess each variable. All constructs, except for firm size, exhibited Cronbach's alpha values exceeding the widely accepted threshold of 0.70, demonstrating strong internal consistency and measurement reliability (Nunnally & Bernstein, 1994). Firm size is not a construct that is measured with a multi-item scale (e.g. number of employees), but an objective, single-item measure, so Cronbach alpha is not applicable. The results reveal that sustainability reporting has a direct, positive, and statistically significant association with firm financial performance. This outcome highlights that organizations practicing transparent and high-quality sustainability reporting tend to achieve superior financial results. These findings are consistent with Stakeholder Theory, which asserts that companies proactively addressing the interests of diverse stakeholders through transparent disclosures are able to cultivate trust, thereby strengthening their reputational standing and financial outcomes (Freeman, 1984; Eccles et al., 2014). The positive association observed is likely attributable to greater stakeholder confidence, improved access to financial resources, and enhanced risk management strategies (Clarkson et al., 2011; Dhaliwal et al., 2011).

**Table 2: Correlations Between Variables**

| Variables | 1 | 2 | 3 | 4 |
|---|---|---|---|---|
| 1. SR | 1 | | | |
| 2. ESG | .65** | 1 | | |
| 3. FP | .59** | .61** | 1 | |
| 4. FS | .31** | .28** | .35** | 1 |

Table 2 presents the correlation analysis among the study variables, demonstrating that all correlations are positive and statistically significant at the 0.01 level. This result indicates meaningful relationships among the variables analyzed. Notably, the strong correlation between sustainability reporting and environmental, social, and governance performance, as well as with financial performance, underscores the interconnectedness proposed by the Resource-Based View. According to this theoretical perspective, environmental, social, and governance practices constitute valuable, rare, and difficult-to-imitate resources that enhance organizational capabilities and contribute to sustained competitive advantage (Barney, 1991; Hart, 1995; Surroca, Tribó, & Waddock, 2010). These findings confirm that sustainability reporting is closely associated with environmental, social, and governance performance and financial outcomes, providing empirical support for the Resource-Based View's explanation of how non-financial resources translate into long-term firm success. All the variables were operationalized using a 5-point Likert scale (1 = Strongly Disagree to 5 = Strongly Agree) except the firm's size which was codified using the number of full-time employees and subsequently standardized.

**Table 3: Regression Analysis for Direct Effects**

| Predictor | B | SE | β | t | p |
|---|---|---|---|---|---|
| Sustainability Reporting (SR) → FP | 0.42 | 0.05 | .43 | 8.40 | < .001 |
| SR → ESG | 0.54 | 0.04 | .65 | 13.50 | < .001 |
| ESG → FP | 0.27 | 0.06 | .29 | 4.50 | < .001 |

Table 3 presents the regression coefficients, which illustrate the direct relationships among the study variables. Sustainability reporting emerges as a robust predictor of environmental, social, and governance performance and firm financial performance. In addition, environmental, social, and governance performance is found to be a significant predictor of financial performance, thereby confirming the study's direct effect hypotheses. These findings also lend support to Legitimacy Theory, which posits that organizations disclose sustainability-related information as a means of aligning with prevailing social norms and expectations. The *B* coefficients are unstandardized effects and they show how the dependent variable changes with a unit change in the predictor. The standardized beta indicates the strength of relationships and the t-value, along with the p-value, indicates statistical significance. By doing so, organizations seek to maintain their legitimacy, safeguard their reputation, and ensure their continued financial strength (Suchman, 1995; Deegan, 2002). The results underscore the importance of transparent sustainability disclosures not only for achieving legitimacy in the eyes of stakeholders but also for enhancing firm performance.

**Table 4: Mediation Analysis (ESG as Mediator)**

| Path | Effect | Boot SE | 95% CI (LL, UL) |
|---|---|---|---|
| SR → ESG → FP (Indirect) | 0.15 | 0.03 | (0.09, 0.22) |
| Total Effect (SR → FP) | 0.42 | 0.05 | (0.32, 0.52) |
| Direct Effect (SR → FP) | 0.27 | 0.06 | (0.15, 0.39) |

Table 4 provides a summary of the mediation analysis results, utilizing bootstrapped confidence intervals. The findings show that the indirect effect of sustainability reporting on financial performance, mediated by environmental, social, and governance performance, is statistically significant. Specifically, the bootstrapped confidence interval for the indirect effect does not include zero, confirming partial mediation. Notably, the magnitude of the indirect effect surpasses that of the direct effect, suggesting that environmental, social, and governance performance accounts for a substantial portion of the relationship between sustainability reporting and financial performance. This result is consistent with previous research, which argues that robust environmental, social, and governance performance transforms sustainability initiatives into measurable financial benefits (Fatemi, Fooladi, & Tehranian, 2015; Garcia, Mendes-Da-Silva, & Orsato, 2017). Organizations excelling in environmental, social, and governance practices achieve greater operational efficiency and improved perceptions among investors, reinforcing the Resource-Based View's assertion that intangible resources such as environmental, social, and governance capabilities drive sustained competitive advantage. The mediation analysis was performed through the PROCESS macro (Model 4) by Hayes (2018) with 5,000 bootstrapped resamples to approximate confidence intervals and indirect effects. Bootstrapping provides more accuracy and does not assume anything about the sampling distribution.

**Table 5: Moderation Analysis (Firm Size as Moderator)**

| Predictor | B | SE | B | t | p |
|---|---|---|---|---|---|
| SR | 0.29 | 0.07 | .32 | 4.14 | < .001 |
| FS | 0.18 | 0.06 | .19 | 3.00 | < .01 |
| SR × FS (Interaction Term) | 0.11 | 0.04 | .19 | 2.75 | < .01 |

Table 5 displays the results of the moderation analysis. The interaction effect between sustainability reporting and firm size on financial performance was found to be statistically significant and positive. This finding suggests that firm size moderates the relationship, indicating that larger organizations demonstrate a stronger association between sustainability reporting and financial performance. Such evidence supports the argument that organizational capabilities, which are typically more developed in larger firms, enhance the ability to implement, communicate, and derive value from sustainability strategies (Aragón-Correa & Sharma, 2003; Orlitzky, Schmidt, & Rynes, 2003). Larger companies possess higher visibility, a broader array of stakeholders to address, and greater resource flexibility, which together facilitate improved alignment with both Legitimacy Theory and Stakeholder Theory. To interpret it, a plain slope plot of the interaction effect (SR x FS) is suggested. This would depict the relationship between sustainability reporting and financial performance to be stronger in larger sizes of the firm. The results of hypothesis testing are to be corresponded with a properly numbered list (e.g., H1, H2, H3a, H3b), as well as with the regression and mediation/moderation tables. Make sure that the numbering in the methods and results sections is the same and referred to in the discussion appropriately.

**Table 6: Summary of Hypothesis Testing**

| Hypothesis | Statement | Result |
|---|---|---|
| H1 | ESG disclosure quality → Firm financial performance | Accepted |
| H2 | ESG disclosure quality → Investor trust | Accepted |
| H3 | Investor trust → Firm financial performance | Accepted |
| H4 | ESG disclosure quality → Investor trust → Firm financial performance | Accepted |
| H5 | Regulatory environment × ESG disclosure → Firm financial performance | Accepted |

### 5.1. Discussion

#### 5.1.1. Stakeholder Perspective and Theoretical Integration

The findings of this research deliver significant additions to the body of the literature investigating the relationship between sustainability reporting and corporate financial performance and confirm and expand a number of existing theoretical constructs. This study, by placing environmental, social, and governance (ESG) performance as the mediating variable and firm size as the moderating factor, not only supports the commonly accepted theoretical viewpoints but also puts them into perspective in terms of application to the practical issues that are unique to developing economies like that of Pakistan. Such a combined methodology provides subtle information on the manner in which sustainability reporting creates financial performance and the manners in which organizational features moderate such associations. The theoretical discussion is based on the Stakeholder Theory, initially developed by Freeman (1984), who argued that corporations will not be able to survive in the long term unless they satisfy the expectations of a wide range of stakeholders, including not only shareholders. The identified positive correlation between sustainability reporting and financial performance aligns with the Stakeholder Theory, in which case the increased clarity on ESG activities increases stakeholder confidence and leads to better financial performance. A host of stakeholders such as investors, customers, regulatory agencies as well as civil society organizations now demand increased accountability and ethical performance by corporations. With systematic ESG reporting, businesses will be able to develop goodwill, strengthen their support base, and improve operations and financial performance. These conclusions are supported by the investigation of Cheng, Green, and Ko (2022) whose proactive ESG engagement results in higher legitimacy, greater access to capital, and additional loyalty among investors in emerging markets characterized by institutional gaps.

#### 5.1.2. Resource-Based View and Size of the Firm

Beyond the Stakeholder Theory, the study offers empirical support to the Resource-Based View (RBV), which argues that sustainable competitive advantage is a result of the possession of valuable, rare, inimitable, and non-substitutable resources (Barney, 1991). The firm size effect obtained in the current analysis implies that Bigger is better placed to embrace and use sustainability practices due to its huge resources. The benefits include financial flexibility, more talented specialization, and leading technologies that allow these firms to produce extensive sustainability reporting that meets the regulatory demand and has strategic advantages. The observation is consistent with the study by Shawat et al. (2024), which shows that in the Middle East and North African regions, the effect of ESG disclosures is strongly determined by the firm size, where larger companies obtain higher financial benefits from sustainability activities.

#### 5.1.3. Legitimacy Theories and Institutional Theories

The research also promotes Legitimacy Theory under corporate sustainability. Legitimacy Theory holds that organizations should carry out their activities in ways that conform to the norms and values in the wider society to achieve and maintain legitimacy (Suchman, 1995). In those jurisdictions where regulatory demands are escalating and people are more conscious about their needs like in Pakistan, sustainability reporting is getting into prominence as a means of institutionalizing responsible business conduct. The results indicate that companies that have strong ESG disclosures have higher chances of preserving legitimacy in the eyes of stakeholders and retaining their operating licenses. The given observation has been supported by Alsayegh, Rahman, and Homayoun (2022), who have stated that, in developing economies, ESG disclosures play a critical role in promoting transparency, fulfilling international standards, and fulfilling institutional needs. The other theory that is applicable to the sustainability reporting scenario is the Institutional Theory. It assumes that organizations tend to follow given norms and structures to become legitimate and stable. With the emergence of sustainability reporting, which is getting more codified with frameworks such as the Global Reporting Initiative and integrated reporting standards, companies in developing economies are faced with the need to adopt the practice. The study shows that institutional alignment can provide not only a legitimacy advantage but also a competitive advantage particularly where this conformity is backed up by stakeholder expectations and robust internal competencies.

#### 5.1.4. ESG as an Intermediary in the Sustainability--Financial Performance Connection

Another important aspect of the current research is that it sheds some light on the mediating role of ESG performance regarding the connection between sustainability disclosure and financial performance. The results emphasize that it is important not only to report about sustainability efforts but to have actual ESG results. This enhances theoretical knowledge by demonstrating that the monetary advantages of sustainability reporting are attained indirectly by means of good ESG performance and favorable stakeholder perceptions. Although the previous studies, such as Sunny and Apsara (2024), had recognized the ability of ESG metrics to impact financially, this piece elucidates the existing confusion by proving the fact that sound ESG performance is vital to achieving the financial benefit of sustainability disclosure. Sunny and Apsara (2024) underline that integrating ESG values into the organization's mission will develop a sustainable culture, increase employee interest, and generate better financial results in the long term. This way a more exquisite model of corporate sustainability is formed where transparency and substantive performance work together in the generation of organizational value. This observation also forms part of the Contingency Theory in sustainability literature which holds that the effectiveness of management approaches is linked to the harmonization of organizational variables and environmental circumstances. The current findings show that the economic impact of sustainability reporting depends on the firm-specific characteristics, including its size, and the quality of ESG performance.

#### 5.1.5. Intermediating Effect of Firm Size: Managerial Implications

The boundary condition of the firm size has practical implications to organizations of any size. Bigger companies, having more resources and competence, can more easily apply the existing sustainability models, like the Global Reporting Initiative or the Sustainability Accounting Standards Board. Such organizations are more visible and have greater stakeholder pressure, allowing them to take greater advantage of ESG reporting. It is recommended, however, that smaller firms engage in flexible, affordable ESG, such as specific programs and custom initiatives. The findings of Shawat et al. (2024) highlight the possibility of small and medium-sized enterprises (SMEs) to enjoy the stakeholder goodwill and improved performance as a result of targeted ESG investments. Mainstream companies, because of their visibility, are expected to avoid separating sustainability goals and business strategies, and sustainability reporting must demonstrate a real organizational commitment. The lack of comprehensive frameworks in most developing regions also leads to an inconsistent non-comparable ESG disclosures. It is recommended that regulators should enforce a disclosure standard and create industry templates and provide incentives including tax relief or green financing to encourage best practices. According to Rahman and Saeed (2021), the inclusion of sustainability in the regulatory landscape boosts the confidence of investors and promotes ethical corporate practices.

#### 5.1.6. Investor/Stakeholder Implications

These findings can also be beneficial to investors and other financial professionals. With the rise of ESG metrics at the center of investment analysis, the question of the relationship between sustainability and financial performance becomes more and more important to measure correctly. The mediated effect in this case underlines the importance of investors to consider the existence and the content of sustainability disclosures. Real-time ESG data is recommended to be used by investment methodologies and rating agencies that should distinguish between genuine reporting and compliance. Alsayegh et al. (2022) describe the usefulness of ESG scores in financial analysis as an area where traditional information might be lacking in representing long-term risk. Shareholder engagement, proxy voting, and sustainability-linked instruments are the methods that institutional investors should consider in order to affect the corporation's behavior. Another important implication is concerning organizational capacity building. The revealed positive correlation between sustainability initiatives and company performance implies that targeted investments in employee training, leadership, and interdisciplinary cooperation are required. It is suggested that companies should establish specific sustainability offices, offer related training, and pursue ESG goals in all operations of the organizations. It corroborates the ideas of

Sunny and Apsara (2024) who insist on the cultivation of a sustainability culture with the help of leadership and the participation of personnel.
Lastly, the results suggest the incorporation of sustainability indicators into the performance management systems. Firms can measure their progress towards ESG goals by embracing the essential performance indicators in this regard. The broader financial objectives should incorporate objectives of reducing carbon emissions, community involvement, employee welfare, and good governance. The balancing of the balanced scorecard to include ESG aspects allows a long-term view of performance measurement and ensures that short-term performance is not pursued at the cost of long-term sustainability.

## 6. Conclusion and Recommendations

The study positively confirmed and statistically significantly the effect of environmental, social, and governance (ESG) disclosure on firm financial performance, especially due to the increased investor confidence and the presence of efficient regulatory frameworks. This research examined the impact of environmental, social, and governance disclosure on firm financial performance, with a particular focus on investor confidence and the influence of regulatory frameworks. The analysis supports the view that comprehensive and transparent environmental, social, and governance disclosure enables firms to achieve superior financial outcomes. Key benefits identified include higher profitability, increased investor attraction, and enhanced firm value in the marketplace. The credibility of sustainability reporting is strengthened when disclosures are transparent and comprehensive, leading stakeholders to respond more positively. The findings reveal that investor confidence acts as an essential link in this relationship, as higher standards of ethical and transparent conduct reinforce investor trust and, in turn, result in greater financial returns for the company. Additionally, the study finds that regulatory structures and legal standards play a significant role in shaping the relationship between environmental, social, and governance performance and financial outcomes. Effective governance and robust regulatory frameworks further enhance the advantages for companies committed to sustainability. These insights highlight the necessity for organizational support and commitment to achieving meaningful environmental, social, and governance reporting and integration. Overall, the results explain that sustainability reporting can significantly improve firm performance in emerging markets. The research contributes to the broader discussion of corporate responsibility by demonstrating that environmental, social, and governance factors are vital not only for compliance but also for securing strategic advantage. In the current era of socially responsible business practices, adopting sustainability-oriented approaches has become fundamental to ensuring long-term corporate success.

### 6.1. Recommendations

Within the Pakistani developing financial ecosystem, businesses are recommended to encompass ESG practices as a part and parcel of their overall strategy as well as operations. The industry-specific ESG frameworks that meet the Securities and Exchange Commission of Pakistan (SECP) requirements and international standards like GRI or SASB would help to enhance the credibility and consistency of the disclosures. Based on these findings, companies are encouraged to integrate environmental, social, and governance practices as core components of both their strategic and operational activities. Firms should treat environmental, social, and governance considerations as fundamental elements within their performance evaluations and everyday managerial decisions. Establishing specialized environmental, social, and governance teams, providing ongoing training for employees, and adhering to internationally recognized reporting standards will enhance internal transparency across the organization. The adoption of widely accepted methodologies and technologies can increase the credibility of reports and facilitate meaningful comparisons across different industries. The implementation of these strategies is expected to foster greater investor confidence, elevate the firm's reputation, and strengthen internal governance.
Additionally, leveraging technology can enable companies to deliver more accurate and efficient environmental, social, and governance disclosures. Utilizing digital dashboards, real-time data monitoring and advanced analytical tools will support precise and timely reporting. Pakistan Policymakers should consider requiring ESG disclosures of listed companies via rule-based systems and providing tax benefits to sustainability implementations. Measures such as preferential lending to green projects, and reg sandboxes to ESG innovation can encourage the greater involvement of corporates in sustainability practices. When evaluating investment opportunities, investors should place emphasis on environmental, social, and governance indicators in conjunction with financial metrics. They should review sustainability ratings and employ active ownership strategies to critically assess company practices. Moreover, further research is needed to examine the long-term impact of environmental, social, and governance integration across various national and industry contexts, as the response to sustainability initiatives may differ between sectors and geographic regions. Besides, there is a need to carry out more studies that would look at the longitudinal effects of ESG integration in sectors including manufacturing, banking, and technology in Pakistan and other similar emerging markets. Future research can be conducted in terms of a mixed-method or case-based approach to reveal organizational behavior, stakeholder responses, and obstacles to ESG implementation on the firm level.

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