

STRATEGIC FINANCIAL MANAGEMENT

A Managerial Approach

Edited by

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Strategic Financial Management

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INVESTOR IN PEOPLE

‘To our cherished families, whose boundless love, unwavering support and enduring encouragement have not only shaped our journey but have also inspired the pages of this book. With heartfelt gratitude and profound admiration, we dedicate these words as a token of our appreciation for the pillars of strength that you are’.

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Preface

*Muhammad Ali, Leong Choi-Meng, Syed Ali Raza, Chin-Hong Puah,
Premagowrie Sivanandan*

Greetings to every individual embarking on the perceptive voyage outlined in '*Strategic Financial Management: A Managerial Approach*'. This research book proves to be a useful companion, providing a careful road map through the complex landscape of modern finance. Financial managers face difficulties in the dynamic business environment of today, and this book provides genuine thoughts and tactics that thoughtfully solve those challenges. Financial managers find themselves at the nexus of tradition and innovation in a period characterised by rapid transformations. More than just a guide, this research book seeks to be a reliable partner for anyone negotiating the challenges of making financial decisions in a setting that necessitates flexibility and critical thinking. The environmental, social and governance (ESG) elements and sustainability have become increasingly important, causing a significant change in the financial landscape. This book explores the relationship between value generation, effective corporate governance and sustainability reporting from a managerial standpoint. Its objective is to provide managers with the knowledge and skills necessary to reconcile profit-driven financial objectives with morally and responsibly conducted businesses. Managers need to re-evaluate international finance plans considering the ways that globalisation has changed the business landscape.

This book rises to the occasion, giving managers navigating the global financial arena insightful perspectives on the opportunities and challenges presented by globalisation. This book examines techniques for controlling financial risks in the face of technical breakthroughs in the digital age, where opportunities and threats abound, particularly in financial risk management. The goal is to provide managers with the tools they need to prosper in the digital age, not just get by. As they are the backbone of economies, small- and medium-sized enterprises (SMEs) require a special approach to financial regulation. A special chapter that offers theoretical frameworks and useful consequences for managers, entrepreneurs and policymakers tackles the unique problems that SMEs encounter. The capacity to gather, process and evaluate information is an essential managerial skill in a world where 'data is king'. This book examines data analytics and management in the finance industry, providing insights into using data to make well-informed decisions – a critical ability in today's data-driven business climate.

The dynamic nature of regulatory environments presents a challenge to compliance. The chapter on regulatory changes and compliance challenges explores how changing regulations affect financial management and provides guidance on how to deal with the difficulties associated with compliance. Building trust and transparency requires effective stakeholder connections and financial communication. A special chapter looks at ways to build positive connections with stakeholders. The final section of our journey across these pages looks at making financial decisions in erratic and unpredictable markets. Managers must have ways to make wise judgements that endure market swings in a volatile and unpredictable environment. This book invites you to go out on a voyage of exploration, where each chapter reveals a fresh aspect of financials and money management. Whether you are an experienced manager or a novice, the pertinent and insightful information presented in this research book intends to equip you with the skills and understanding required to successfully negotiate the complex curves of today's financial environment.

When you open 'Strategic Financial Management: A Managerial Approach', picture yourself as an avid and involved reader who is actively exploring tips and tactics that can help you to strengthen your current financial success as well as provide useful information to climb out of current financial difficulties. Either way, this research book is here to make strategic financial management more understandable and relatable for you.

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We extend our sincere gratitude to the gifted writers who shaped the story of this book with their commitment, knowledge and teamwork. They are the real designers of this project, and each chapter has benefited from their contributions, which have given it more depth and richness.

We would also like to thank our families for being our steadfast source of support and for giving us the time and space we needed to learn about the intricacies of contemporary finance.

We express our gratitude to the hard-working staff of the Emerald publishing team. The dedicated staff of Emerald publishing has played an essential role in transforming concepts into the concrete information that is contained on these pages. We received wonderful support from team Emerald throughout the publishing process.

Finally, we would like to thank all of you, the readers. We are inspired by your dedication to overcoming the obstacles of contemporary finance and your quest for knowledge. We all contributed to this book, and we genuinely hope it will be a useful tool for you as you pursue your managerial goals.

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Chapter 1

Sustainability Reporting, Value Creation and Effective Corporate Governance: A Managerial Perspective

Premagowrie Sivanandan

Taylor's University, Malaysia

Abstract

Sustainability reporting has gained momentum in recent years, especially with the enhanced attention paid by market participants and regulators to environmental, social and governance (ESG) practices. This chapter discusses the interconnected link between sustainability reporting and ESG and helps readers comprehend how businesses evaluate and communicate their social performance (i.e. ESG) and financial performance (i.e. economic) to businesses' key stakeholders. This chapter also reviews the inclusion of corporate governance into the presumably simple yet certainly complex sustainability reporting–ESG–corporate governance mix that provides businesses with the opportunities to do good in the pursuit of financial success and sustainable growth. Additionally, sustainability reporting that reports authentic ESG practices in the presence of effective corporate governance also helps to enhance a company's public image, attract investors, reduce risks and contribute to environmental and societal well-being. The successful integration of sustainability reporting and ESG with traditional financial reports, thus, is in the hands of managers who are expected to lead in the best interest of the company's shareholders and other stakeholders. Effective corporate governance, therefore, is seen as crucial for this convergence to create value, promote economic growth and address environmental and social concerns for long-term growth and sustainability.

Keywords: Sustainability; sustainability reporting; ESG; environmental; social; governance; economic; corporate governance

1. Introduction

The concept of sustainability's most widely used definition is 'Development that meets the needs of the present without compromising the ability of future generations to meet their own needs' (Brundtland, 1987, p. 41). Brundtland (1987) further describes that sustainability encompasses the concept of 'needs' and the idea of 'limitations'. The concept of 'needs' prioritizes the necessities of the world's impoverishment for which top emphasis should be accorded. On the other hand, the idea of 'limitations' refers to the notion that the status of technology and social structure places constraints on the environment's capacity to meet current and future needs of the world's population. On the other hand, Székely and Knirsch (2005) describe sustainability as economic growth, shareholder value, prestige, corporate reputation, customer relationships, and the quality of products and services that are sustainable and constantly expanding. This definition of sustainability also entails implementing and upholding moral corporate conduct, generating long-term employment opportunities, adding value for all parties involved in the company and meeting the needs of the underprivileged. The notion of sustainability, which has become one of the driving forces that spur companies to attain financial growth and success, must thus be measurable for managers, regulators and other stakeholders to assess how sustainability is achieved and the extent of success of the companies' sustainable practices. This brings us to sustainability reporting, also known as triple-bottom-line reporting, corporate social responsibility (CSR) reporting, ESG reporting, non-financial reporting and sustainable development reporting (Siew, 2015).

Sustainability has become such an integral part of business, both locally and globally, that regulators, companies and governments have taken numerous proactive steps and meaningful actions to adopt sustainability reporting in their national and international agenda. This is primarily due to the constant pressure for improved sustainability or ESG practices from a variety of stakeholders, including institutional investors, lenders, customers, non-governmental organizations and regulators, as well as disclosures from businesses (*Bursa Malaysia Sustainability Reporting Guide*, 2022). Ensuring that businesses operate responsibly, ethically and sustainably while also enhancing the communities in which they operate is the aim of corporate sustainability. Corporate sustainability may ensure successful and socially responsible business operations by addressing a range of issues, including reducing greenhouse gas (GHG) emissions, improving labour standards, safeguarding the environment and furthering human rights (HSBC, 2023). Malaysia, for example, through its Ministry of Investment, Trade and Industry (MITI) is taking a significant step towards sustainability and its goal of reaching net-zero emissions by 2050 with the introduction of the *Industry Environmental, Social and Governance (iESG) Framework* (Tan, 2023). The iESG framework could potentially be a key factor in assisting Malaysia in meeting its sustainability targets within a seven-year timeframe and gaining access to the US\$12 trillion global ESG market (Tan, 2023). From the global perspective, the *Global Reporting Initiative (GRI)* released the revised *GRI Standards 2023*, which provide companies with a reference point and guide to prepare integrated ESG reports or standalone sustainability/non-financial reports. Nevertheless,

challenges arise in the form of economic upheavals, natural disasters such as floods and earthquakes and political instability, which threaten to deter companies from executing their sustainable initiatives and reporting with sustainable practices fairly and equitably.

Companies, therefore, must negotiate a challenging terrain in the constantly evolving field of corporate governance, one that is characterized by environmental obstacles, stakeholder demands and economic uncertainties, to maneuver the complex yet rewarding practice of sustainability reporting. In a time of increased environmental consciousness and changing public expectations, the combination of sustainable reporting with sound corporate governance has become essential for companies all over the world. Sustainable practices, thus, are investments for the future that can support core business objectives rather than merely duties or campaigns of public relations (NST Business, 2023). [Ernst and Young \(2023\)](#) elucidate that achieving sustainability is essential to the fight against climate change, achieving the 17 *United Nations Sustainable Development Goals (UNSDGs)* (also known as ‘Agenda 2030’) and building a more equitable society. The nexus between corporate governance and sustainable reporting in the modern business context offers managers and business leaders a dynamic environment to attain financial success ‘with a heart’.

In today’s economic environment, managers are essential in guiding companies towards the attainment of sustainability and long-term profitability while maintaining strong corporate governance standards. This is supported by [ACCA \(2023\)](#), which states that a company’s reputation, positive innovation and eventually profitability are largely determined by how the company handles its non-financial challenges, e.g. environmental and social challenges. The benefits of integrating sustainability into business are numerous, and this should motivate managers of Malaysian businesses, publicly listed companies and small and medium enterprises (SMEs) alike to expand their sustainability initiatives to enjoy advantages such as improving risk management, fostering creativity, stimulating the entry of new customers, boosting output, reducing expenses, building brand value and reputation, and maintaining an operating licence. However, despite the growing trend and emphasis on the importance of sustainability, an alarming 45% of Malaysian corporates and SMEs admit to not allocating a budget for their sustainability initiatives (*Malaysia Businesses Sustainability Pulse Report 2022*), which brings us to question the role of managers in ensuring sustainable reporting for their companies. According to *FTSE Russell*, the overall ESG score for Malaysian companies in 2022 was 2.5 out of 5, and this represents a 33.7% increase in the overall ESG score of Malaysian companies since 2018 (*The Edge Malaysia, 2023*). Even though there is a notable improvement in how publicly listed companies in Malaysia are implementing and reporting their sustainability initiatives, the overall ESG score of 50% shows that there is still considerable room for improvement in terms of how the companies manage their ESG facets of the business.

The ‘E’ in ESG stands for ‘Environmental’, which refers to the influence of an organization on ecosystems, air, water, lands and other living and non-living natural systems, such as the use of water and energy, emissions released into the atmosphere and loss of biodiversity. The ‘S’ in ESG is ‘Social’, which makes references to the effects that an organization has on the social structures in which

it functions including the organization's ties to the community, its workers and its clients. The 'G' in ESG, on the other hand, is defined as 'Governance', which refers to the governance aspects of decision-making in an organization, ranging from policymaking to the allocation of rights and obligations among various corporate stakeholders (*GRI G4 Sustainability Reporting Guidelines*), such as the C-suite (i.e. the CEO, COO, CFO and CIO), managers, employees, customers, shareholders and the board of directors. However, conflicting perceptions about ESG pose a challenge on the road towards achieving sustainability due to factions that perceive ESG or sustainable practices to be a form of 'greenwashing' with zero impact by companies that try to paint a positive picture to 'hide' their environmentally damaging business activities. These factions such as environmental activists and civil society organizations observe that companies' managers are not entirely honest about the companies' ESG efforts, and some companies tend to overstate their sustainability efforts with a hidden agenda (Tan, 2023). Hence, the role of managers in nurturing sustainability reporting through effective corporate governance becomes more prominent due to the need to ascertain whether the companies are actually 'walking the talk' and are engaging in sustainable practices for the good of the environment and society. The managerial viewpoint on how governance procedures and strategic decision-making support sustainable reporting is, hence, discussed in this chapter. This chapter also explores the mutually beneficial relationship between sustainable reporting and corporate governance and how important a role they play in forming ethical and resilient businesses in the future.

2. Literature Review

2.1 Sustainability Reporting and ESG: The Road Towards Value Creation

Sustainability and ESG are two concepts that are correlated with each other yet display distinct characteristics. The evaluation of a company's effects on the environment, society and governance is conducted using a set of criteria known as ESG. According to Evanson (2023), the adoption of ESG principles can lead to long-term value creation and a better future for the planet, people and businesses (i.e. profit). The three pillars of ESG are provided in the indicative list in Table 1.1 below:

Table 1.1. ESG Pillars With Indicative Constituents.

E (Environment)	S (Social)	G (Governance)
Climate change	Human rights	Board independence
Carbon emission	Labour standards	Board diversity
Pollution	Poverty	Transparency
Resource erosion	Equal health opportunities	Shareholders' participation
Biodiversity	Equal Education	Employee wellness
Green coverage	Social security	Equal opportunity

Source: A Review of ESG Performance as a Measure of Stakeholders' Theory, Kumar (2023).

Sustainability, on the other hand, emphasizes the capacity to persist in the long run using the interaction between a business' environmental, social and economic aspects (HSBC, 2023). The goal of environmental sustainability is to minimize GHG emissions, cut back on waste and pollution and conserve natural resources to reduce or eliminate adverse effects on the environment. The social component prioritizes human rights, community involvement, health and safety, and fair and safe labour practices to advance social fairness, diversity and inclusion. Finally, the economic side of sustainability is concerned with preserving long-term profitability, generating economic value and assuring prudent resource allocation. ESG, thus, can be considered a subset of sustainability that embraces the economic facets of a business. The primary distinction between sustainability and ESG is that the latter is a wide concept that includes a variety of ethical business practices, whereas ESG is a particular approach used to assess a company's environmental, social and economic performance. ESG indicators are, thus, employed to assess how well a company is performing in specific domains, such as executive remuneration, diversity and inclusion and carbon emissions (HSBC, 2023).

A company's report regarding the ESG impacts of its operations is known as a sustainability report or ESG report. The sustainability report makes it viable for the business to communicate its possibilities and risks more openly to its shareholders and other stakeholders and acts as a communication tool to persuade cynics and doubtful parties that the company's actions are sincere (PwC, 2023). As sustainability is a broad, multifaceted and rarely measurable concept, ESG provides a precise quantitative measure of a company's sustainability and corporate social performance, making it possible to better understand how sustainability practices affect the measurable results of a business's financial and operational performance (Clark & Viehs, 2014) through sustainability reporting. McBride Sustainability (2023) states that sustainability reporting can benefit companies and society by lowering risks, boosting stakeholder participation and increasing transparency. Zumente and Bistрова (2021) affirm that managers of businesses with greater knowledge of sustainability ensure that shareholders' value is created through enhanced financial performance, better management and lower risk indicators. Furthermore, qualitative non-financial characteristics like reputation, stakeholders' trust, employee satisfaction and engagement have also been found to have an even greater impact on long-term value (Zumente & Bistрова, 2021). Through the participation of external stakeholders and regulators in the process, sustainability reporting enables companies to publish transparent, current and verifiable information on ESG performance (World Business Council for Sustainable Development, 2018). The importance of sustainability reporting in corporate Malaysia has steered *Bursa Malaysia* to disclose in September 2022 that publicly listed companies in Malaysia would be required to report on sustainability more comprehensively with the gradual implementation of the reporting rules with the first financial year end in 2023. This strategy provides enlightening insights that *Bursa Malaysia* has tightened its disclosure requirements to encourage Malaysian public listed companies to embrace and share sustainable practices that might boost organizational resilience and competitiveness in luring additional capital to

assist the shift to net zero (Ernst & Young, 2022) and subsequently leading to long-term value creation.

Value creation has become inclusive, and creating long-term shareholder value is no longer exclusive to only shareholders. Even though the phrase ‘shareholder value’ was originally coined primarily to represent an emphasis on short-term returns, it is now increasingly used to highlight the necessity for managers of companies to act sustainably and ethically to secure the companies’ place in the economy in the long run (Bistrova & Lace, 2012). Value creation, thus, has evolved to include satisfying the needs of other stakeholders as well such as managers, suppliers, customers and employees. In the same vein, Henisz et al. (2019) find that a sound ESG proposition opens the door to enhanced value creation that encompasses exceptional financial growth through better access to resources, reduction in costs due to lower energy consumption, legal and regulatory intervention through government support and subsidies and increased production capacity due to boost in employee morale. Friske et al. (2023) further attest that when businesses learn how to better communicate sustainability objectives to stakeholders and investors learn how to correctly evaluate financial reports and sustainability reports, sustainability reporting, which is initially a costly signal, ultimately enhances company value. To phrase it simply, sustainability reporting through ESG measures focuses on how companies can create value for all their stakeholders including the expected financial returns for their shareholders. Thus, managerial commitment and altruistic behaviour are important to drive efficient and effective planning and decision-making for value creation through the institutionalization of sustainability reporting. However, it is also vital to note that not all sustainable practices are conducted to do good, and managers may engage in sustainable activities to hide the company’s misdeeds and portray an ‘angelic’ front to shareholders and other stakeholders. This is supported by Zimon et al. (2022) who affirm that managers are driven to act morally and socially to try to cover up the company’s errors and improve its standing in the eyes of shareholders and other stakeholders.

2.2 Sustainability Reporting and Corporate Governance: Making It Work

Sustainability reporting incorporates ESG considerations in addition to financial gains. Sustainability reporting, thus, transcends beyond financial indicators as sustainable reporting represents a company’s overall financial performance and social performance taking ESG factors into account. As more Malaysian businesses realize the link between sustainability reporting, long-term financial viability and ESG performance, the incorporation of sustainable practices into business models is gaining traction. In this context, corporate governance completes the sustainability reporting–value creation–ESG mosaic by serving as a facilitator to guarantee that business strategies are in line with sustainable ideals.

Corporate governance refers to the mechanisms and internal controls that are put in place in a company to ensure that the company is managed in an ethical and accountable manner to attain maximisation of shareholders’ wealth.

Corporate governance creates a three-fold structure for transparency, ethics and accountability within a company. According to [Boiral and Henri \(2017\)](#), corporate governance considers every interest that has an impact on the competence, morality and viability of an organization. It is imperative for businesses that aim to succeed in the long run to mandatorily embrace sustainable practices in corporate governance. Managers are, thus, urged to think about the wider effects of their strategic decisions and choices on the environment, society and governance rather than only concentrating on financial success. In other words, sustainability reporting transcends beyond the bottom line. According to [L'Huillier \(2014\)](#), under the auspices of agency theory, the connotative definition of 'corporate governance' relates to enforcement strategies used to oversee the actions and decisions of managers who are 'agents' selected by the company's 'principal', i.e. the shareholders. The need to oversee the actions and decisions made by managers stems from the notion that managers are motivated to manage their companies' earnings to boost performance-linked remuneration that is linked to firm equity value especially when specific performance targets are required to be achieved or maintained before the managers can enjoy the fruits of their labour ([Sivanandan & Abdul Wahab, 2020](#)). This in turn can impair the quality of earnings reported in the financial statements when managers' actions and decisions are driven by opportunism and greed rather than altruism for the benefit of the company's shareholders and other stakeholders, which in turn can affect the quality of sustainability reporting. It is, therefore, the responsibility of managers to preserve moral principles, guarantee openness and promote an accountable culture within their companies in the pursuit of wealth and financial gains.

Effective corporate governance entails the implementation of sound corporate governance mechanisms, such as board diversity, audit committee, institutional ownership and executive and non-executive remuneration, to ensure the company is managed fairly and ethically. Extant literature (for example, [Beji et al., 2021](#); [Masud et al., 2018](#); [Mudiyansele, 2018](#); [Ong & Djajadikerta, 2018](#)) shows that there is a positive relationship between sustainability reporting and corporate governance, which exhibits that good corporate governance drives sustainability reporting, which in turn results in value creation for companies. For example, [Githaiga and Kosgei \(2023\)](#) discover a positive and significant correlation between sustainability reporting and board independence, gender diversity and financial expertise because board characteristics are essential to quality financial reporting, voluntary disclosure and reduction in information asymmetries. Similarly, [Perrault and McHugh \(2015\)](#) and [Cormier and Magnan \(2015\)](#) explain that the board of directors is compelled to earn, preserve and fix a company's legitimacy by promoting transparency and advocating disclosure of the company's social and environmental performance through sustainability reporting. This is underpinned by the legitimacy theory ([Dowling & Pfeffer, 1975](#)), which proposes that companies engage in the disclosure of their CSR information to present a virtuous and socially responsible image to legitimize their corporate and social behaviour to the companies' multiple stakeholders. This is supported by [Ntim and Soobaroyen \(2013\)](#) who assert that a diverse board can advance a company's

legitimacy by reaching out to a larger range of stakeholders and fostering stronger bonds between the company and its constituents.

Sustainability reporting, which is an integral element of financial reporting, acts as a stakeholder engagement tool that helps to validate a company's corporate ethical behaviour to its shareholders and other stakeholders. In line with this, [Buallay et al. \(2020\)](#) find that the level of ESG disclosure via sustainability reporting increases when the presence of females on the board of directors increases. Additionally, [Ahmad et al. \(2018\)](#) claim that directors with a background in finance and training in social accounting are more aware of the significance of social and environmental issues, and are therefore, more likely to support the company's sustainability reporting efforts due to the high priority they place on society and the environment. Similarly, [Ong and Djajadikerta \(2017\)](#) find that the proportion of independent directors, multiple directorships and the presence of females on the board of directors is significantly and positively correlated with sustainability reporting and disclosures. [Olayinka et al. \(2022\)](#), on the other hand, report that audit expertise, frequency of audit committee meetings and audit committee size are significantly and positively related to sustainability reporting in Nigerian public listed companies. This is because the audit committee of a company oversees financial reporting procedures, chooses the company's independent auditor and receives both internal and external audit results from the internal and external auditors.

Institutional ownership refers to the ownership of shares in firms that are held by financial and non-financial institutions. Institutional investors act as the agents of corporate governance in their capacity as large shareholders who are deemed to possess the ability and power to mitigate the agency problem that arises between a firm's managers and its shareholders through monitoring of managers' behaviour, actions and decision-making process. The *Malaysian Code for Institutional Investors 2014* regards institutional investors as major players in the global economy due to the significant influence that institutional investors exert over the firms they invest in (i.e. 'investees') arising from their large shareholdings in the firms (Minority Shareholders Watch Group, 2014). It is, thus, expected that institutional investors play a key role in driving sustainability reporting in their investee firms through sound corporate governance. [Alomran and Alsaahli \(2023\)](#) find that long-term institutional investors significantly affect the reliability of companies' sustainability reports through external assurance. This is due to the long-term institutional investors' oversight role and a keen interest in long-term financial performance as opposed to short-termism which usually attracts short-term institutional investors. [Strampelli and Balp \(2023\)](#) in the same vein assert that institutional investors are the primary users of sustainability reporting because measuring the impact of sustainability practices implemented by investee companies is becoming more and more important to evaluate how ESG elements affect firm profitability and risk, and consequently, the overall returns on their investment portfolios.