Economic and Business Horizon

ISSN: 2963-2765

Economic and Business Horizon
Volume: 05
Issue: 04
Year: 2026
Page: 443-458

Citation:
Suari, D. P. A., Yuniarta, G. A., & Musmini, L. S. (2026). The effect of ESG and financial constraints on cost of equity: Institutional ownership as a moderating variable. *Economic and Business Horizon, 5*(4), 443-458.

The Effect of ESG and Financial Constraints on Cost of Equity: Institutional Ownership as a Moderating Variable

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Abstract

Environmental, Social, and Governance (ESG) disclosure and financial constraints influence investors' risk perceptions and the cost of equity, yet the moderating role of institutional ownership remains inconclusive. This study examines the effects of ESG disclosure and financial constraints on the cost of equity, as well as the moderating role of institutional ownership, among non-primary consumer companies listed on the Indonesia Stock Exchange. A quantitative approach was employed using balanced panel data from 63 companies during 2022–2024 (189 firm-year observations). The study employed the CAPM, ESGDI, SA Index, and institutional ownership ratio to measure the variables. The data were analyzed using random-effects panel regression with robust standard errors clustered and the firm level and moderated regression analysis in Stata. The results show that ESG disclosure significantly reduces the cost of equity, whereas financial constraints significantly increase it. However, institutional ownership does not significantly moderate the effects of ESG disclosure or financial constraints on the cost of equity. These findings suggest that investors place greater emphasis on sustainability disclosure and firms' financial conditions than on ownership structure when evaluating investment risk. The study provides evidence that strengthening ESG disclosure and maintaining financial flexibility are effective strategies for reducing equity financing costs in emerging markets.

Keywords

Cost of Equity, ESG Disclosure, Financial Constraints, Institutional Ownership.

1. Introduction

The Indonesian consumer cyclical sector has faced increasing pressure, reflecting heightened investor concerns over firms' profitability and risk exposure. Since early 2025, the sector has declined by 11.09%, despite positive growth in the Composite Stock Price Index, suggesting that firm-specific uncertainty rather than overall market conditions has driven its weak performance. Rising uncertainty regarding future earnings increases investors' required returns, thereby elevating the cost of equity (Natalia et al., 2021; Supriono, 2022). Investor risk perception is commonly reflected in the Price-to-Earnings Ratio (PER), where a lower PER indicates higher expected returns due to greater earnings uncertainty (Yana & Agustiningsih, 2022). This condition is evident among Indonesian consumer cyclical firms, which experienced substantial earnings volatility during 2021–2025. Such instability reduces earnings reliability, complicates cash flow projections, and increases the equity risk premium demanded by investors, ultimately constraining long-term investment capacity and competitiveness (Ghazi et al., 2024).

Beyond financial performance, investors increasingly rely on non-financial information to assess corporate risk (Rahmasari, 2013; Nazir et al., 2022; Qian, 2024). Environmental, Social, and Governance (ESG) performance has emerged as an important indicator of transparency, governance quality, and long-term sustainability, with stronger ESG performance generally associated with lower perceived risk and a lower cost of equity (Javaid et al., 2023; Sandberg et al., 2023). In Indonesia, the temporary suspension of Morgan Stanley Capital International (MSCI) index rebalancing due to concerns over ownership transparency and free-float disclosure underscored the importance of governance quality and information transparency in strengthening investor confidence. Consistent with this view, ESG disclosure and environmental cost management improve market valuation, reduce perceived risk, and facilitate access to external financing (Tang, 2022; Putu & Devi, 2024). Pellegrini et al. (2019), Chouaibi et al. (2021), and Rao (2023) consistently documented a negative relationship between ESG performance and the cost of equity in the oil and gas industry.

While ESG captures non-financial sources of investment risk, investors also evaluate firms' financial conditions, particularly their ability to access external financing. Financial constraints increase liquidity risk, cash flow uncertainty, and the risk premium required by investors, thereby raising the cost of equity (Robiansyah et al., 2020; Anggreni & Robiyanto, 2021). Constrained firms are also more vulnerable to financial distress during economic shocks, limiting their capacity to undertake long-term investments (Budiari & Devi, 2023). Consistent with this view, financially constrained firms generally face higher expected returns and equity financing costs because investors demand greater compensation for financing risk (Livdan et al., 2009; Syarif et al., 2019). However, favorable institutional conditions, such as tax incentives, may alleviate financing constraints and reduce the cost of equity, suggesting that this relationship remains context-dependent, particularly in emerging markets (Chen et al., 2011; Dai et al., 2013).

The inconsistent findings suggest that additional governance mechanisms may shape how investors interpret ESG performance and financing conditions. Institutional ownership is one such mechanism because institutional investors possess stronger monitoring capabilities, broader access to information, and a long-term investment orientation (Ali et al., 2023; Ni & Yin, 2023; Huang et al., 2024). Their monitoring role strengthens corporate governance, reduces information asymmetry, discourages greenwashing, and enhances the credibility of financial and non-financial disclosures (Gustyana & Hanari, 2022; Elly et al., 2024). Consequently, institutional ownership is expected to moderate the effects of ESG performance and financial constraints on the cost of equity by increasing market confidence and

lowering investors' perceived risk (Purwanti & Mulya, 2023; Putrandy & Santoso, 2025). Firms with stronger institutional ownership are therefore likely to elicit different investor responses to ESG quality and financing constraints than firms with weaker institutional monitoring.

Despite extensive research on ESG and the cost of equity, empirical findings remain inconsistent, particularly in emerging markets. Indonesian studies have also largely focused on financial constraints in relation to capital structure and debt financing, with limited attention to their effects on the cost of equity. Furthermore, few studies have simultaneously examined ESG performance and financial constraints while considering institutional ownership as a moderating governance mechanism, particularly in the consumer cyclical sector. Accordingly, this study examines the effects of ESG performance and financial constraints on the cost of equity of consumer cyclical firms listed on the Indonesia Stock Exchange. It investigates whether institutional ownership moderates these relationships.

2. Literature Review and Hypothesis Development

2.1. The Effect of ESG on Cost of Equity

ESG performance is an important indicator of how firms manage non-financial risks, including environmental, social, and governance issues. From the perspective of Stakeholder Theory, firms are accountable not only to shareholders but also to a broader range of stakeholders, including governments, employees, communities, and investors. Companies that effectively meet stakeholder expectations through sound ESG practices are more likely to gain social legitimacy and strengthen investor confidence. Moreover, from the perspective of Information Asymmetry Theory, ESG disclosure serves as a credible signal that reduces information asymmetry between managers and investors (Ramirez et al., 2022).

Transparent ESG information enables investors to assess corporate risk more accurately, thereby lowering the risk premium they require and ultimately reducing the firm's cost of equity (Brusov & Filatova, 2025). Empirical evidence consistently supports this negative relationship. Che et al. (2024) found that firms with stronger ESG performance exhibit lower costs of equity due to greater transparency and reduced investor risk perception. Similar findings were reported by Mathath et al. (2025) and Wang et al. (2025), who demonstrated that improved ESG disclosure lowers firms' equity financing costs. Furthermore, Christensen et al. (2021) showed that enhanced non-financial transparency effectively mitigates information asymmetry in capital markets, reducing investors' required risk premiums. In economically sensitive industries such as the consumer cyclical sector, sustainability investments also signal long-term corporate resilience, which plays a critical role in shaping investors' required returns, particularly in emerging markets (Zhou, 2025).

H1: ESG has a negative and significant effect on cost of equity.

2.2. The Effect of Financial Constraints on Cost of Equity

Financial constraints reflect a firm's limited ability to obtain external financing due to high financing costs, insufficient collateral, or uncertainty regarding future performance. From the perspective of Information Asymmetry Theory, financially constrained firms generally face greater information uncertainty, making it more difficult for investors to accurately evaluate future cash flows and corporate prospects. This uncertainty increases perceived investment risk, leading investors to demand higher expected returns and, consequently, a higher cost of equity. Moreover, from the perspective of Stakeholder Theory, financial constraints indicate a firm's limited capacity to maintain stable relationships with key financial stakeholders, including investors and creditors (Valentinov & Chia, 2022). Restricted

access to external financing increases liquidity risk and cash flow uncertainty, thereby weakening stakeholder confidence and raising investors' required risk premiums. Costa et al. (2021) further argued that financing constraints intensify information asymmetry and reduce firms' operational flexibility, reinforcing investors' concerns over future financial performance.

Similarly, Luo et al. (2015) suggested that difficulties in accessing external financing constrain firms' ability to pursue profitable investment opportunities, thereby increasing perceived financial risk. Consistent with these arguments, Hu and Wang (2025) demonstrated that financing constraints are positively associated with higher costs of equity because investors interpret uncertainty in external financing as an additional source of systematic risk requiring greater compensation. Consequently, firms operating under severe financing constraints are more likely to face higher equity financing costs, particularly in industries that are highly sensitive to fluctuations in consumer demand and economic cycles (Chen et al., 2011).

H2: Financial constraints have a positive effect on the cost of equity.

2.3. Institutional Ownership as an ESG's Moderator

From the perspective of Agency Theory, institutional investors possess stronger monitoring capabilities than individual shareholders, enabling them to mitigate agency conflicts and improve corporate transparency. Their active oversight encourages managers to adopt higher standards of governance and sustainability disclosure, thereby enhancing the credibility of ESG reporting (Ali et al., 2023; Rahman et al., 2023). Consistent with Stakeholder Theory, firms with superior ESG practices are more likely to gain legitimacy and trust from stakeholders. However, the ability of ESG performance to reduce the cost of equity is expected to be stronger when supported by institutional investors who ensure that sustainability practices are implemented substantively rather than merely as symbolic disclosures. Empirical evidence supports this moderating role. Yahia et al. (2023) found that institutional ownership strengthens the negative relationship between ESG performance and the cost of equity by improving information credibility and enhancing managerial monitoring.

Institutional investors, particularly those with long-term investment horizons, tend to apply stringent sustainability criteria in portfolio selection while demanding greater transparency in non-financial reporting to reduce information asymmetry. This governance mechanism was further confirmed by Pertiwi and Setiawan (2024), who showed that institutional ownership reinforces the positive effect of ESG disclosure in reducing market risk perceptions within the consumer cyclical sector. Likewise, Yip (2025) argued that professionally monitored ESG implementation enhances corporate efficiency, transparency, and reputation, providing greater assurance that sustainability practices are genuine rather than opportunistic. Consequently, stronger institutional oversight increases investor confidence, lowers perceived risk, and further reduces firms' cost of equity.

H3: Institutional ownership moderates the relationship between ESG and the cost of equity.

2.4. Institutional Ownership as a Financial Constraints' Moderator

From the perspective of Agency Theory, institutional investors possess superior monitoring capabilities that reduce agency conflicts by overseeing managerial behavior and improving the quality of corporate decision-making. Their active involvement enhances corporate reputation in capital markets and strengthens the confidence of other investors. Furthermore, from the perspective of Information

Asymmetry Theory, institutional ownership reduces information uncertainty by improving the credibility and transparency of corporate disclosures (Jensen & Meckling, 1976; Akerlof, 1978). As a result, investors are better able to assess firms' financial conditions, thereby reducing the perceived risk associated with financial constraints. Accordingly, institutional ownership is expected to weaken the positive effect of financial constraints on the cost of equity by enhancing corporate credibility and facilitating access to external financing.

Although the market often interprets limited financing opportunities as signals of high liquidity risk and financial vulnerability, the presence of institutional shareholders provides a positive signal regarding governance quality and financial stability (Hwang & Kim, 2024). Lewellen and Lowry (2025) demonstrated that institutional ownership significantly alleviates financing constraints by improving firms' ability to raise capital in equity markets. Similarly, Ni and Yin (2023) found that strong institutional ownership reduces the cost of equity by mitigating agency conflicts and enhancing financial reporting transparency. Through stronger governance, greater disclosure credibility, and more effective monitoring, institutional investors alleviate market concerns over firms' financing limitations, thereby reducing the risk premium required by investors and mitigating the increase in the cost of equity resulting from financial constraints.

H4: Institutional ownership moderates the relationship between financial constraints and the cost of equity.

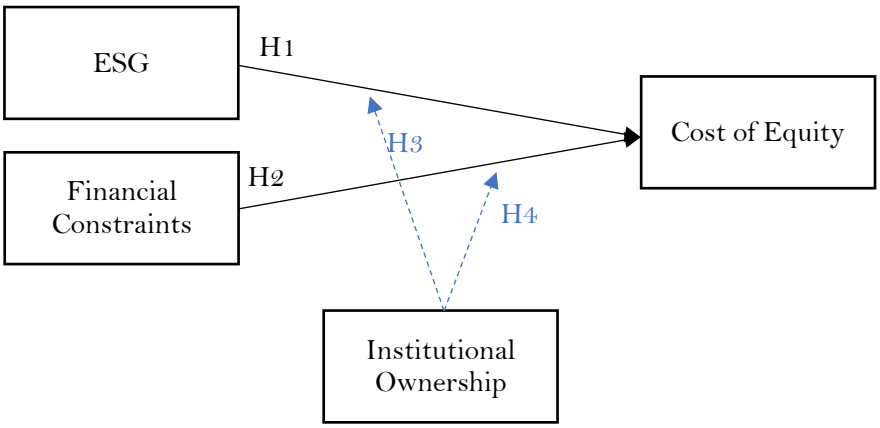

Figure 1. Research Framework

Figure 1 illustrates the conceptual relationships among ESG, financial constraints, institutional ownership, and cost of equity. The framework shows that ESG has a negative effect on cost of equity, while financial constraints have a positive effect on cost of equity. Institutional ownership acts as a moderating variable that influences the relationship between ESG, financial constraints, and cost of equity.

3. Methods

This study employed a quantitative research approach to examine the effects of ESG performance and financial constraints on firms' cost of equity, with institutional ownership as a moderating variable. A quantitative approach was selected because it enables objective and systematic analysis of numerical data for hypothesis testing and causal inference. Data were analyzed using Stata, which supports multiple linear regression, moderation analysis, and robustness testing. Accordingly, this study is classified as causal-comparative research with a descriptive-analytical design.

The study focused on consumer cyclical companies listed on the Indonesia Stock Exchange because this sector is highly sensitive to market perception and sustainability-related reputation, making the effects of ESG performance and financial constraints on the cost of equity more pronounced. The research was conducted from January to June 2026, using panel data covering the 2022–2024 period, including annual reports, ESG scores, and institutional ownership data.

The population comprised 148 consumer cyclical firms listed on the Indonesia Stock Exchange. A purposive sampling technique was applied to ensure data consistency and reliable estimation of the cost of equity. Firms were excluded if they (1) were under special monitoring (22 firms), (2) experienced trading suspension (17 firms), (3) were listed after 2021 (25 firms), or (4) lacked a valid beta estimate required for the Capital Asset Pricing Model (1 firm). After excluding 65 firms, the final sample consisted of 83 companies, resulting in balanced panel data for the 2022–2024 period. These firms were subsequently analyzed to examine the effects of ESG performance and financial constraints on the cost of equity, as well as the moderating role of institutional ownership.

The dependent variable, cost of equity, is measured using the Capital Asset Pricing Model (CAPM) developed by Sharpe (1964) and Lintner (1965). ESG performance is measured using the ESG Disclosure Index (ESGDI) based on the Global Reporting Initiative (GRI) framework through content analysis of 30 disclosure items (Dhaliwal et al., 2011; Dua & Sharma, 2024; Zhou et al., 2025). Financial constraints are measured using the Size-Age (SA) Index, which captures firms' constraints in accessing external financing based on firm size and age (Hadlock & Pierce, 2010; Whited & Wu, 2006). The moderating variable, institutional ownership (INST), is measured as the percentage of outstanding shares held by institutional investors, representing the level of external monitoring and corporate governance (Shleifer & Vishny, 1986; Bushee, 1998; Drobetz et al., 2024; Rivandi et al., 2024).

Data were analyzed using Stata with a panel data approach and Moderated Regression Analysis (MRA). The analysis began with descriptive statistics, followed by correlation and multicollinearity tests using the Variance Inflation Factor (VIF). Panel model selection was conducted through the Chow, Hausman, and Breusch–Pagan Lagrange Multiplier (LM) tests to determine the most appropriate estimation model. The hypotheses were then tested using panel regression with interaction terms, while cluster-robust standard errors were employed to address heteroskedasticity and autocorrelation. Statistical significance was evaluated at the 5% significance level ($p < 0.05$).

4. Results

The panel data initially consisted of 83 consumer cyclical firms selected through purposive sampling. Following the preliminary data screening, 20 firms were excluded because they produced negative cost of equity values resulting from negative stock beta estimates in the CAPM. Since a negative cost of equity is considered financially anomalous, these observations were removed to improve model stability and avoid estimation bias caused by outliers. Consequently, the final sample comprised 63 firms observed over the 2022–2024 period, yielding a strongly balanced panel with 189 firm-year observations and no missing data. This balanced structure ensures the reliability of the subsequent panel regression analysis.

Table 1. Descriptive Statistics

Variable	Observations	Mean	Standard Deviation	Minimum	Maximum
Cost of Equity (Y)	189	0.0673	0.0248	0.0005	0.1829
ESG Disclosure Index (X1)	189	0.8437	0.0238	0.8016	0.8900
Financial Constraints (X2)	189	-2.2171	0.7975	-3.8611	-0.0771
Institutional Ownership (Z)	189	64.0270	23.2909	0.0000	99.5600

Table 1 presents the descriptive statistics for the 189 firm-year observations. The average cost of equity is 0.0673 (6.73%), ranging from 0.0005 to 0.1829, with a relatively low standard deviation (0.0248), indicating limited variation in investors' required returns across the sample. The mean ESG Disclosure Index is 0.8437, with values ranging from 0.8016 to 0.8900, suggesting consistently high ESG disclosure among consumer cyclical firms. Financial constraints, measured by the SA Index, have a mean of -2.2171 and range from -3.8611 to -0.0771, indicating substantial variation in firms' access to external financing, where values closer to zero represent greater financing constraints. Meanwhile, institutional ownership averages 64.03%, ranging from 0% to 99.56%, with a relatively high standard deviation (23.2909), reflecting considerable heterogeneity in ownership structures across the sampled firms. The descriptive statistics indicate sufficient variation in the explanatory variables while maintaining a relatively stable distribution of the dependent variable, supporting the suitability of the dataset for subsequent panel regression analysis.

Table 2. Correlation Test

Variable	Cost of Equity	ESG	Financial Constraints	Institutional Ownership
Cost of Equity	1.0000			
ESG Disclosure	-0.1554*	1.0000		
	(0.0327)			
Financial Constraints	0.5182*	0.0300	1.0000	
	(0.0000)	(0.6816)		
Institutional Ownership	-0.1487*	0.2651*	-0.0217	1.0000
	(0.0411)	(0.0002)	(0.7665)	

Table 2 reports the Pearson correlation matrix among the study variables. ESG disclosure is negatively correlated with the cost of equity ($r = -0.1554$, $p = 0.0327$), indicating that firms with higher ESG disclosure tend to face lower equity financing costs. In contrast, financial constraints exhibit a positive and statistically significant correlation with the cost of equity ($r = 0.5182$, $p < 0.001$), suggesting that firms experiencing greater financing constraints are associated with higher investor-required returns. Similarly, institutional ownership is negatively correlated with the cost of equity ($r = -0.1487$, $p = 0.0411$), implying that stronger institutional monitoring is associated with lower equity financing costs.

The correlations among the explanatory variables are generally weak. ESG disclosure is positively associated with institutional ownership ($r = 0.2651$, $p = 0.0002$), whereas the relationships between ESG disclosure and financial constraints ($r = 0.0300$, $p = 0.6816$) and between financial constraints and institutional ownership ($r = -0.0217$, $p = 0.7665$) are statistically insignificant. Furthermore, all pairwise correlation coefficients are well below the commonly accepted threshold of 0.80, indicating that multicollinearity is unlikely to be a concern in the subsequent regression analysis.

Table 3. Multicollinearity Test

Variable	VIF	Tolerance (1/VIF)
Institutional Ownership	1.24	0.8096
ESG Disclosure X Institutional Ownership	1.15	0.8692
ESG Disclosure	1.09	0.9180
Financial Constraints X Institutional Ownership	1.05	0.9545
Financial Constraints	1.02	0.9786
Mean VIF	1.11	—

Table 3 presents the results of the multicollinearity test using the VIF and tolerance values. All variables, including the interaction terms, exhibit VIF values ranging from 1.02 to 1.24, while the corresponding tolerance values range from 0.8096 to 0.9786. Furthermore, the mean VIF is 1.11, which is substantially below the commonly accepted threshold of 10. Likewise, all tolerance values exceed the minimum threshold of 0.10. These results indicate that the regression model is free from multicollinearity, suggesting that the explanatory variables are sufficiently independent and that the estimated coefficients can be interpreted reliably in the subsequent panel regression analysis.

Table 4. Hausman Test Results

Test Statistic	Value
Chi-square (χ^2)	6.22
Degrees of Freedom	5
Probability > χ^2	0.2855
Decision	Fail to reject H_0
Selected Model	Random Effects Model (REM)

Table 4 presents the results of the Hausman test, which was performed to determine whether the Fixed Effects Model (FEM) or the Random Effects Model (REM) was more appropriate for estimating the panel data. The null hypothesis states that there is no systematic difference between the coefficients estimated by the two models, implying that the REM provides more efficient and consistent estimates. The decision criterion is based on the probability value, where a *p*-value greater than 0.05 indicates that the REM should be selected.

The test produced a chi-square statistic of 6.22 with 5 degrees of freedom and a probability value of 0.2855. Since the *p*-value exceeds the 5% significance level, the null hypothesis cannot be rejected, indicating that the coefficient differences between the FEM and REM are not systematic. Accordingly, the REM was selected as the most appropriate estimation model for the subsequent panel regression analysis.

Table 5. Model Statistics Model 1 & 2

Statistic	Model 1	Model 2
Number of observations	189	189
Number of groups	63	63
Wald $\chi^2(3)$	38.67	43.60
Prob > χ^2	0.0000	0.0000
Sigma_u	0.0124	0.0125
Sigma_e	0.0168	0.0168
Rho	0.3533	0.3569
R-Squared Within	0.2893	0.2893
R-Squared Between	0.3232	0.3292
R-Squared Overall	0.3048	0.3083

Table 5 presents the random-effects regression results for the baseline and moderated models, estimated using clustered robust standard errors to account for

heteroscedasticity and within-firm autocorrelation. In Model 1, the Wald χ^2 statistic of 38.67 ($p < 0.001$) indicates that ESG performance, financial constraints, and institutional ownership jointly have a significant effect on the cost of equity. The model explains 30.48% of the variation in the dependent variable (Overall R^2 = 0.3048), while the remaining 69.52% is attributable to factors outside the model. The constant term is positive and statistically significant ($\beta = 0.0673$, $p < 0.001$), indicating a positive baseline level of the cost of equity after controlling for the explanatory variables.

Model 2 extends the baseline specification by incorporating the interaction terms between institutional ownership and both ESG performance and financial constraints. The model remains jointly significant, with a Wald χ^2 of 43.60 ($p < 0.001$), confirming that the explanatory variables and their interaction effects collectively influence the cost of equity. The inclusion of the moderating variables slightly improves the model's explanatory power, increasing the Overall R^2 from 0.3048 to 0.3083, indicating that the full model explains 30.83% of the variation in the cost of equity. The constant also remains positive and significant ($\beta = 0.0669$, $p < 0.001$), suggesting that the baseline level of the cost of equity remains positive after accounting for the moderating effects.

Table 6. Hypothesis test Model 1 & 2

Model	Variable	Coefficient	Std. Error	z-value	p-value	95% CI
1	ESG Disclosure	-0.2082	0.0906	-2.30	0.022	[-0.3858, -0.0307]
	Financial Constraints	0.0168	0.0036	4.70	0.000	[0.0098, 0.0238]
	Institutional Ownership	-0.0009	0.0007	-1.17	0.243	[-0.0022, 0.0006]
	Constant	0.0673	0.0020	33.92	0.000	[0.0634, 0.0711]
2	ESG Disclosure	-0.2145	0.0857	-2.50	0.012	[-0.3825, -0.0466]
	Financial Constraints	0.0166	0.0035	4.72	0.000	[0.0097, 0.0235]
	Institutional Ownership	-0.0001	0.0003	-0.84	0.404	[-0.0021, 0.0009]
	ESG × Institutional Ownership	0.0024	0.0034	0.71	0.477	[-0.0043, 0.0091]
	Financial Constraints × Institutional Ownership	0.00003	0.00013	0.21	0.837	[-0.00022, 0.00027]
	Constant	0.0669	0.0020	34.17	0.000	[0.0631, 0.0707]

As reported in Table 6, the partial regression results indicate that ESG performance has a significant negative effect on the cost of equity ($\beta = -0.2082$, $p = 0.022$), suggesting that firms with higher ESG performance tend to face lower equity financing costs. Conversely, financial constraints exert a significant positive effect on the cost of equity ($\beta = 0.0168$, $p < 0.001$), indicating that firms experiencing greater financing constraints require higher expected returns from investors. Meanwhile, institutional ownership does not have a significant direct effect on the cost of equity ($\beta = -0.0001$, $p = 0.243$).

The moderation analysis further reveals that institutional ownership does not significantly moderate the relationship between ESG performance and the cost of equity ($\beta = 0.0024$, $p = 0.477$) or between financial constraints and the cost of equity

($\beta = 0.00003$, $p = 0.837$). These findings indicate that institutional ownership neither strengthens nor weakens the effects of ESG performance and financial constraints on the cost of equity among Indonesian consumer cyclical firms.

5. Discussion

The findings indicate that ESG performance is negatively associated with the cost of equity, suggesting that firms with stronger environmental, social, and governance practices are perceived as less risky by investors and therefore require lower expected returns. This result is consistent with Stakeholder Theory, which argues that firms creating value for a broad range of stakeholders strengthen their legitimacy and enhance investor confidence. It is also supported by Asymmetric Information Theory, whereby transparent ESG disclosure reduces information asymmetry and uncertainty regarding firms' long-term prospects, leading investors to demand lower risk premiums. These findings are consistent with previous studies by Che et al. (2024) and Mathath et al. (2025), which documented that superior ESG disclosure reduces the cost of equity through enhanced transparency and lower perceived risk. Similarly, the evidence aligns with Jafar et al. (2024), who found that ESG disclosure among Indonesian non-financial firms mitigates idiosyncratic risk and lowers investors' required returns. Collectively, these findings suggest that ESG practices should be viewed not only as a sustainability commitment but also as a strategic mechanism for improving financing efficiency by reducing equity financing costs.

In contrast, financial constraints increase the cost of equity, indicating that firms with limited access to external financing are perceived as riskier and therefore face higher required returns. This finding is consistent with the financing constraints framework of Fazzari et al. (1988), which argues that restricted financing capacity limits investment opportunities and increases financial risk. The result is further supported by Stakeholder Theory and Asymmetric Information Theory, suggesting that financing constraints weaken stakeholder confidence and increase information asymmetry, leading investors to demand higher risk premiums. These findings are consistent with Syarif et al. (2019) and Costa et al. (2021), confirming that financially constrained firms generally incur higher equity financing costs due to greater perceived risk.

The moderation analysis indicates that institutional ownership does not significantly moderate the relationship between ESG performance and the cost of equity. This finding suggests that investors evaluate ESG disclosure primarily based on its intrinsic quality rather than the ownership structure of the firm. From the perspective of Stakeholder Theory, institutional investors are expected to strengthen corporate governance and enhance the credibility of sustainability practices through effective monitoring. Likewise, Asymmetric Information Theory argues that institutional investors should reinforce the informational value of ESG disclosure by reducing information asymmetry. However, the insignificant moderating effect implies that ESG disclosure itself already serves as a sufficiently credible market signal, making additional monitoring by institutional investors less influential in shaping investors' required returns (Waheed et al., 2021). This result contrasts with Yahia et al. (2023), who documented a significant moderating role of institutional ownership, but is consistent with the Indonesian market context, where ESG information appears to be priced directly by investors regardless of institutional ownership concentration, thereby limiting the governance-enhancing role suggested by Pertiwi and Setiawan (2024) and Yip (2025).

Similarly, institutional ownership fails to moderate the relationship between financial constraints and the cost of equity, indicating that strong institutional ownership is insufficient to offset the adverse impact of financing constraints on investors' risk perceptions. This finding suggests that investors place greater

emphasis on firms' fundamental financial conditions, such as liquidity and financing capacity, than on ownership structure when determining required returns. Although Agency Theory proposes that institutional investors improve governance and facilitate access to external financing, and prior studies by Lewellen and Lowry (2025) and Ni and Yin (2023) suggest that institutional ownership can alleviate financing frictions through enhanced monitoring and transparency, such mechanisms were not supported in this study. A plausible explanation is that, in the Indonesian consumer cyclical sector, financial constraints constitute a strong fundamental risk signal that cannot be mitigated solely by institutional monitoring. Consequently, investors continue to demand higher risk premiums despite the presence of institutional shareholders, indicating that corporate financial fundamentals remain more influential than ownership structure in determining the cost of equity.

6. Conclusion

This study investigates the effects of ESG disclosure and financial constraints on the cost of equity of 63 non-primary consumer companies listed on the Indonesia Stock Exchange during 2022–2024, with institutional ownership as a moderating variable. The findings indicate that ESG disclosure significantly reduces the cost of equity by improving transparency and reducing information asymmetry, thereby lowering investors' perceived risk. In contrast, financial constraints significantly increase the cost of equity, as firms with limited access to external financing are viewed as riskier and consequently face higher required returns. However, institutional ownership does not significantly moderate the relationships between ESG and the cost of equity or between financial constraints and the cost of equity, suggesting that ownership structure alone is insufficient to alter investors' risk assessments in the Indonesian capital market.

These findings imply that strengthening ESG practices and maintaining financial flexibility are important strategies for reducing financing costs and enhancing market confidence. For regulators, the results highlight the importance of improving ESG disclosure standards and promoting greater transparency to support sustainable capital markets. This study is limited to non-primary consumer firms listed on the Indonesia Stock Exchange during the 2022–2024 period. It employs the SA Index to measure financial constraints, which may limit the generalizability of the findings. Future research is encouraged to examine broader industry sectors, extend the observation period, compare alternative financial constraint measures, and explore other governance mechanisms, such as foreign institutional ownership, board characteristics, or ownership concentration, that may better explain variations in the cost of equity.

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