

THE INFLUENCE OF EARNINGS MANAGEMENT ON CORPORATE RISK WITH ESG AS A MODERATION VARIABLE

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Abstract

The low quality of financial reporting due to earnings management practices can increase information uncertainty, reflected in the volatility of stock returns as an indicator of corporate risk. On the other hand, the application of Environmental, Social, and Governance (ESG) principles is expected to increase transparency, accountability, and the quality of corporate governance, thereby mitigating risks arising from opportunistic management behavior. However, empirical evidence on the role of ESG in moderating the relationship between earnings management and corporate risk, particularly in the banking sector in post-pandemic Indonesia, is still limited. This study aims to examine the influence of earnings management on corporate risk, proxied by stock return volatility, and to analyze the role of ESG disclosure as a moderating variable in banking companies listed on the Indonesia Stock Exchange for the 2022-2024 period. The study used a quantitative method and purposive sampling, yielding 120 company-year observations from 40 banking companies. Hypothesis testing was performed using a panel data multiple linear regression. The study's results show that earnings management does not significantly affect stock return volatility. Moreover, ESG disclosures are not able to moderate the relationship between earnings management and corporate risk. These findings indicate that the volatility of stock returns in banking firms during the observation period was influenced more by factors beyond earnings management practices and ESG disclosures. The implications of this study emphasize the importance of strengthening the quality of ESG implementation, financial reporting transparency, and corporate governance to support more effective risk management.

Keywords: Earnings Management, Corporate Risk, ESG, Banking Sector

1. Introduction

Corporate risk is one of the main concerns for investors when assessing a company's sustainability and stability. Corporate risk can affect a business's success or failure, so the company must manage it effectively. Corporate risks arise not only from internal operational conditions but also from market perceptions of the uncertainty of corporate performance and managerial decisions (Bachtiar et al., 2025). The banking sector plays an important role in assessing corporate risks because banks collect and distribute public funds. The stability of the banking sector is very important to the national economy because disruptions in banks' performance can undermine public confidence, deter investment, and destabilize the financial system. The banking sector is the backbone of a healthy financial system and is the main instrument in the national economy. However, banking activities are also inherent in various risks, such as credit risk, market risk, operational risk, and capital risk (Agustina & Rahmatika, 2024; Qin, 2024).

One of the prominent risks in the banking sector is credit risk, as reflected in Non-Performing Loans (NPLs). The Financial Services Authority (OJK) has established NPLs as one of the main indicators of bank health and a barometer of credit risk management. The OJK also requires that NPLs be kept within prudent limits to maintain the stability of the national financial system and investor confidence in the resilience of banking fundamentals (Otoritas Jasa Keuangan, 2017). During the COVID-19 pandemic, credit risk increased as many debtors experienced income pressure and difficulty meeting loan obligations. Based on the data, the total non-performing loans of national banks reached the highest number (Kusnandar, 2021). However, these conditions began to improve in the post-pandemic period, indicating that in 2024, Indonesian banks' bad-loan levels will reach their lowest level in the last five years (Ahdiat, 2025). The relationship between credit risk and corporate risk lies in how investors perceive information about asset quality, credit risk, and the bank's performance prospects. The recovery in credit risk indicators has not fully eliminated investor uncertainty, as the market continues to assess banks' condition based on the quality of financial information and stock price movements. Thus, credit risk dynamics can evolve into market-based corporate risks, as reflected in stock return volatility.

The main problem in this study is the uncertainty of corporate risk in the banking sector, which is reflected through the volatility of stock returns. These risks are influenced not only by the bank's operational conditions but also by the quality of financial information available to investors. When financial information does not fully reflect a company's economic condition, investors may have difficulty accurately assessing a bank's performance, prospects, and risks. Therefore, it is important to examine factors that can affect a company's risk, including earnings management. Previous research has shown inconsistent results regarding the influence of earnings management on corporate risk. Azzahra & Achyani (2024) found that earnings management had no influence on corporate risk. This finding is consistent with Agustia et al. (2020), who show that earnings management does not affect corporate risk. However, Prakosa et al. (2022) found different results showing that earnings management can increase corporate risk. This research is supported by research findings that earnings management can affect a corporate risk profile (Agatha & Fathoni, 2025; Ameralya & Pramesti, 2024). The differences in the study's results indicate that the relationship between earnings management and corporate risk still needs further study, especially in the Indonesian banking sector in the post-pandemic period (Jasman & Murwaningsari, 2022).

In addition to earnings management, environmental, social, and governance (ESG) factors are also important in explaining corporate risks. ESG reflects a company's commitment to governance, transparency, accountability, social responsibility, and environmental sustainability. Empirical research shows that broader ESG disclosures can lower corporate risk, including specific, systematic, and bankruptcy risks (Holm & Pettersson, 2026). Research also shows that ESG disclosures can reduce corporate risks by providing positive signals to investors about the quality of risk management (Febriani & Machmuddah, 2026). Earnings management has distinctive characteristics because it can be achieved through discretion in credit loss reserve policy. The reserve policy contains elements of estimation and management considerations, thus providing room for management to influence the reported profit. When reserves are set not entirely based on actual economic conditions, the practice may indicate earnings management. The greater the discretion management uses in determining reserves, the higher the indication that reported earnings have been influenced by certain accounting policies to flatten profits,

meet performance targets, or maintain positive investor perceptions (Agustia et al., 2020). In this study, ESG is positioned as a moderating variable because it is expected to influence the strength or weakness of the relationship between earnings management and corporate risk. Banks with high ESG disclosures tend to be perceived as having a stronger commitment to transparency, risk control, and quality governance. This commitment can increase the credibility of the information the company conveys, thereby reducing uncertainty due to earnings management practices. In contrast, at banks with low ESG disclosure, earnings management practices may be more readily perceived as a negative signal because supervisory and transparency mechanisms are perceived as weaker. Therefore, ESG can serve as a monitoring mechanism and a governance signal, both of which affect the relationship between earnings management and corporate risk.

Several factors drive the urgency of this research. First, the post-pandemic period (2022-2024) represents a critical phase of economic recovery, normalization of credit restructuring policies, and increased attention to governance and sustainability, making it a relevant context for examining the relationship between earnings management, ESG, and corporate risk. Second, the banking sector plays a strategic role in the national economy, and disruptions in bank performance can affect public confidence, investors, and financial system stability. Third, although credit risk indicators have improved, market-based corporate risk, as reflected in stock return volatility, remains a significant concern for investors. Fourth, the inconsistency of prior research findings on the relationship between earnings management and corporate risk indicates a research gap that warrants attention, particularly in the context of the Indonesian banking sector. Fifth, the role of ESG as a moderating variable in the relationship between earnings management and corporate risk has not been extensively studied, especially in the Indonesian banking sector.

The research gap in this study lies in the limited research examining the influence of earnings management on market-based corporate risk, particularly in the Indonesian banking sector during the post-pandemic period. Most previous research has placed risk more in the context of credit risk, bank stability, efficiency, bankruptcy risk, or bank risk-taking behavior. Meanwhile, research using stock return volatility as a proxy for corporate risk remains relatively limited in the banking context. In fact, the volatility of stock returns reflects the market's response to information uncertainty, earnings quality, performance prospects, and investors' perception of corporate risk. The novelty of this study lies in four main aspects. First, it focuses on the Indonesian banking sector during the 2022–2024 post-pandemic period, a critical phase marked by economic recovery, the normalization of credit-restructuring policies, and an increasing emphasis on corporate governance and sustainability. Second, this study employs the discretionary component of the allowance for impairment losses (CKPN) as a proxy for earnings management, reflecting managerial discretion in estimating expected credit losses within the banking industry. Third, unlike prior studies that primarily examine bank-specific or credit risk, this study measures corporate risk using stock return volatility, thereby capturing investors' market-based perceptions of risk. Fourth, this study incorporates ESG disclosure as a moderating variable to examine whether corporate transparency, governance quality, and sustainability commitment influence the relationship between earnings management and corporate risk.

The purpose of this study is to examine the influence of earnings management on corporate risk and analyze the role of ESG in moderating the relationship between earnings management and corporate risk in banking companies listed on the Indonesia

Stock Exchange for the 2022-2024 period. Specifically, this research aims to: (1) analyze the effect of earnings management on corporate risk; (2) analyze the moderating role of ESG in the relationship between earnings management and corporate risk. This study uses profitability and firm size as control variables. Profitability reflects banks' ability to generate profits from their assets. Banks with higher profitability tend to have more stable financial conditions, greater capacity to absorb risk, and a better ability to maintain investor confidence. This condition can reduce market uncertainty about the company's prospects, so that stock price movements become relatively more stable and stock return volatility tends to be lower. This is consistent with research showing that profitability has a significant negative effect on corporate risk (Ngono & Pone, 2021). This means that the higher the bank's profitability, the lower the corporate risk level because more profitable banks have less pressure to make high-risk decisions and are better able to maintain market confidence. Meanwhile, a bank's size can affect risk exposure, business diversification, access to funding, and the level of market surveillance. Larger banks generally have more complex business structures but also greater resource capacity and market visibility. Chowdhury et al. (2024) explained that bank size plays an important role in bank stability: large banks are better able to manage risks and withstand economic shocks, but they also carry higher systemic risks due to the complexity of their business networks. Therefore, the company's profitability and size need to be controlled to more accurately test the influence of earnings management, ESG, and their interaction on corporate risk.

The contribution of this research is multifaceted. From a theoretical perspective, this research is expected to contribute to the literature on the relationship between earnings management and corporate risk by positioning ESG as a moderating variable. This research also expands the study of corporate risk in the banking sector by using stock return volatility as a market-based proxy for risk. From a practical perspective, this research is expected to benefit bank management, investors, financial analysts, and regulators. For bank management, this study provides an understanding of the importance of transparency in financial reporting and the management of credit loss reserves based on real economic conditions. For investors and financial analysts, this research can be a consideration in assessing the quality of profits, ESG disclosures, and risk profiles of banking companies. For OJK and policymakers, this research can serve as input for strengthening financial reporting supervision and ESG implementation in the banking sector, as part of efforts to improve information quality and corporate risk management.

This article is organized into five sections. Following this introduction, Section 2 presents the theoretical background and hypothesis development, including a review of relevant theories, previous research, and the conceptual framework. Section 3 describes the research methodology, including research design, population and sample, operational definitions of variables, and data analysis techniques. Section 4 presents the results and discussion, including descriptive statistics, classical assumption tests, and hypothesis tests. Finally, Section 5 concludes the study with a summary of findings, implications, limitations, and suggestions for future research.

2. Theoretical Background

2.1 Agency Theory

Agency theory, as articulated by Jensen & Meckling (1976), focuses on contract-based relationships among parties within a business entity or organization, in which the principal delegates decision-making responsibilities to the agent. Both principals and

agents are assumed to be economically rational individuals whose primary motivation is self-interest. However, differences in preferences, beliefs, and information availability can lead agents to behave in self-interested ways that may be contrary to the principal's interests. This divergence of interests creates agency costs, which companies seek to minimize through mechanisms such as effective corporate governance and transparent financial reporting. In the banking context, agency theory holds that management, as an agent, has more information about the company's internal conditions than shareholders, as principals. This condition provides an opportunity for management to exercise accounting discretion, including through the determination of Credit Loss Reserves (CKPN), as this account involves management estimates and considerations when determining potential credit losses. When CKPN is used to flatten profits, meet short-term performance targets, or maintain positive market perceptions, financial statements become less reflective of the bank's actual economic condition. This condition lowers the quality of profits and magnifies information asymmetry because investors cannot accurately assess asset quality, potential credit losses, performance prospects, and corporate risks. Based on agency theory, ESG can serve as a monitoring mechanism that limits management's opportunistic behavior, including earnings management. The better the implementation of ESG, the greater the company's demands to present transparent and accountable information to investors and other stakeholders, thereby reducing information asymmetry and agency costs.

2.2 Stakeholder Theory

Stakeholder theory was first introduced by Freeman (1984) and posits that a company has an inherent obligation to create benefits not only for itself but also for all its stakeholders. These stakeholders encompass a broad spectrum of entities, including investors, creditors, consumers, suppliers, government authorities, the public, analysts, and other related parties. The theory emphasizes that organizational success should be measured not solely by financial performance but also by the company's ability to manage relationships with all stakeholders. In the capital market context, stakeholder trust is strongly influenced by the quality of information the company conveys. Therefore, ESG can be seen as a mechanism that strengthens transparency, accountability, supervisory quality, and the credibility of corporate information. Stakeholder theory provides a robust framework for understanding how ESG practices can limit management's opportunistic behavior, including earnings management, as companies face increasing demands from various stakeholders to present transparent and accountable information. Companies with high ESG disclosure tend to face greater pressure to maintain the credibility of their financial information and meet stakeholder expectations, thereby reducing the potential for opportunistic earnings management.

2.3 Signaling Theory

Signaling theory was initially developed by Spence (1973) to analyze interaction patterns in the labor market, particularly concerning information asymmetry between two parties. In a broad sense, a signal is information issued by a company (management) to external parties (investors). These signals contain important information intended to alter outsiders' perceptions of the company's condition and prospects. The fundamental premise of signaling theory is that management possesses superior information regarding the company's performance and future prospects compared to external stakeholders. Consequently, companies are motivated to convey positive signals through mechanisms

such as ESG disclosures and transparent financial reporting to reduce information asymmetry and enhance market valuation. In the banking context, ESG disclosures serve as positive signals to investors regarding the quality of risk management, transparency, and governance. Banks with high ESG disclosures tend to be perceived as having a stronger commitment to transparency, risk control, and sound governance, which can increase the credibility of the information they convey and reduce uncertainty stemming from Earnings Management practices. When investors receive positive signals through ESG disclosures, they are better able to assess the quality of bank performance and risk, thereby reducing stock return volatility and corporate risk.

2.4 Corporate Risk

Corporate risk is one of the main concerns for investors when assessing a company's sustainability and stability. Corporate risk can affect a business's success or failure, so the company must manage it effectively. Corporate risks arise not only from internal operational conditions but also from market perceptions of the uncertainty of the company's performance and managerial decisions (Bachtiar et al., 2025). In the banking sector, corporate risk encompasses various dimensions, including credit, market, operational, and capital risk (Agustina & Rahmatika, 2024; Qin, 2024). The relationship between credit risk and corporate risk lies in how investors perceive information about asset quality, credit risk, and the bank's performance prospects. The recovery in credit risk indicators has not fully eliminated investor uncertainty, as the market continues to assess banks' condition based on the quality of financial information and stock price movements. Thus, credit risk dynamics can evolve into market-based corporate risks, as reflected in stock return volatility. Corporate risk in this study is measured using stock return volatility, which reflects the market's response to information uncertainty, profit quality, performance prospects, and investors' perception of corporate risk.

2.5 Earnings Management

Earnings management is the practice of influencing reported earnings through accounting discretion to achieve specific objectives. In the banking sector, earnings management has distinctive characteristics because it can be achieved through discretion in credit loss reserve policy. The reserve policy contains elements of estimation and management considerations, thus providing room for management to influence the reported profit. When reserves are set not entirely based on actual economic conditions, the practice may indicate earnings management. The greater the discretion management uses in determining reserves, the higher the indication that reported earnings have been influenced by certain accounting policies to flatten profits, meet performance targets, or maintain positive investor perceptions (Agustia et al., 2020). In this study, earnings management is measured using the discretionary component of the Impairment Loss Reserve (CKPN). This component is obtained from the residual of the CKPN estimation model that normal economic factors, such as credit quality, the business cycle, and credit growth, cannot explain. The residual reflects managerial discretion beyond the actual need for loan loss provisions. When CKPN is used to flatten profits, meet short-term performance targets, or maintain positive market perceptions, financial statements become less reflective of the bank's actual economic condition, thereby lowering the quality of profits and magnifying information asymmetry.

2.6 Environmental, Social, and Governance (ESG)

Environmental, Social, and Governance (ESG) reflects a company's commitment to integrating environmental, social, and governance considerations into its business strategy and operations. ESG disclosure serves as a mechanism through which companies communicate information about their environmental, social, and governance practices to investors and other stakeholders, enabling them to evaluate how companies manage sustainability-related risks and opportunities. Through greater transparency and accountability, ESG disclosure helps reduce information asymmetry, strengthen stakeholder confidence, improve corporate reputation, and support more effective risk management, thereby contributing to long-term corporate sustainability (Wulandari et al., 2026). Based on agency theory, ESG can serve as a monitoring mechanism that limits management's opportunistic behavior, including earnings management. Based on stakeholder theory, ESG reflects a company's responsibility to all parties involved in or affected by its activities, including investors, creditors, regulators, customers, employees, and the public. In the capital market, stakeholder trust is strongly influenced by the quality of information the company communicates, making ESG a critical factor in maintaining investor confidence and reducing corporate risk. Based on signaling theory, ESG disclosures serve as positive signals to investors about the quality of risk management, transparency, and governance, thereby increasing the credibility of the information conveyed and reducing uncertainty stemming from earnings management.

2.7 Hypothesis Development

2.7.1 The Influence of Earnings Management on Corporate Risk

Earnings management in this study was measured using the discretionary component of the Allowance for Impairment Losses (CKPN). This component is obtained from the residual of the CKPN estimation model that cannot be explained by normal economic factors, such as credit quality, the business cycle, and credit growth. The residual reflects managerial discretion beyond the actual need for loan loss provisions. According to agency theory, the relationship between principals and agents can give rise to conflicts of interest due to differences in objectives and information asymmetry (Jensen & Meckling, 1976). Management, as the agent, possesses more information about the company's internal conditions than shareholders, as principals. This information advantage provides management with opportunities to exercise accounting discretion opportunistically. In the banking context, such discretion can be exercised through the determination of CKPN, as this account involves management's estimates and judgments in assessing expected credit losses. When CKPN is used to smooth earnings, achieve short-term performance targets, or maintain favorable market perceptions, financial statements become less representative of the bank's actual economic condition. Consequently, earnings quality declines, information asymmetry increases, and investors face greater difficulty in accurately assessing asset quality, potential credit losses, future performance, and corporate risk.

From the perspective of signaling theory (Spence, 1973), financial statements constitute an important signal through which management communicates the company's financial condition and future prospects to investors. High-quality financial reporting serves as a positive signal that reduces information asymmetry and enhances investor confidence. Conversely, earnings management may weaken the credibility of financial statements because reported earnings no longer fully reflect the firm's underlying economic performance. When investors perceive that reported earnings contain managerial discretion intended to achieve specific objectives, they may interpret this as a

negative signal regarding earnings quality, financial transparency, and future performance. Such negative signals increase uncertainty, reduce investor confidence, and trigger stronger market reactions, ultimately increasing stock return volatility as a proxy for corporate risk.

Consistent with agency and signaling theories, the relationship between earnings management and corporate risk should be viewed from a capital-market perspective. Earnings management can increase corporate risk by undermining the credibility of financial statements and creating uncertainty for investors when assessing banks' fundamental conditions. When investors suspect that reported earnings do not fully reflect a company's actual economic performance, confidence in financial information declines, leading to stronger reactions to unfavorable information and to ambiguous financial signals. Consequently, stock prices become more volatile, and corporate risk increases as reflected in stock return volatility. Thus, earnings management through CKPN is not only associated with internal banking conditions or credit risk but also has broader implications for market-based corporate risk. The higher the level of earnings management, the greater the information uncertainty faced by investors, leading to higher perceived risk, lower market confidence, and greater stock return volatility.

Previous empirical studies generally support this theoretical argument. Vo et al. (2022) reported that earnings management practices are associated with banks' risk profiles, while Jasman & Murwaningsari (2022) documented that Indonesian banks engage in earnings management through CKPN. Furthermore, Agatha & Fathoni (2025), Ameralya & Pramesti (2024), and Prakosa et al. (2022) concluded that earnings management increases corporate risk by reducing the transparency and credibility of financial reporting. Based on these theoretical arguments and empirical findings, earnings management through CKPN is expected to increase corporate risk by reducing earnings quality, intensifying information asymmetry, generating negative market signals, increasing investor uncertainty, and ultimately leading to greater volatility in stock returns. Therefore, the first hypothesis is formulated as follows:

H1: Earnings management has a positive effect on corporate risk

2.7.2 The Moderating Role of ESG on the Relationship between Earnings Management and Corporate Risk

Environmental, Social, and Governance (ESG) represents a framework that integrates environmental, social, and governance considerations into corporate decision-making and sustainability practices (Ozili, 2021). Based on agency theory, ESG serves as a monitoring mechanism that limits management's opportunistic behavior, including earnings management. Strong ESG practices increase management's accountability and reduce information asymmetry by encouraging more transparent and reliable financial reporting. Consequently, companies with higher ESG implementation are expected to face lower agency conflicts because management has fewer opportunities to engage in opportunistic accounting practices.

Stakeholder theory further explains that companies are responsible not only to shareholders but also to a broader group of stakeholders, including investors, creditors, regulators, customers, employees, and society (Freeman, 1984). To maintain stakeholder trust, companies are expected to disclose transparent, credible, and comprehensive information regarding both financial and non-financial performance. ESG disclosure, therefore, reflects corporate accountability and strengthens stakeholder confidence in the firm's governance and long-term sustainability. Companies with stronger ESG

performance are more likely to maintain high-quality financial reporting because they face greater pressure to satisfy stakeholder expectations.

From the perspective of signaling theory (Spence, 1973), ESG disclosure serves as a positive market signal of a company's governance quality, transparency, and commitment to sustainable business practices. High ESG disclosure signals that the company possesses stronger governance mechanisms and more effective internal controls, thereby enhancing the credibility of both financial and non-financial information. Consequently, when investors observe high ESG performance, they may perceive earnings management practices as less indicative of opportunistic behavior because the overall governance environment provides greater assurance regarding the reliability of corporate disclosures. As a result, ESG can reduce investor uncertainty and weaken the negative market reaction associated with earnings management.

Previous empirical studies support these theoretical arguments. Aydoğmuş et al. (2022), Febriani & Machmuddah (2026), and Holm & Pettersson (2026) found that companies with stronger ESG disclosure generally experience lower corporate risk because they exhibit greater transparency, stronger reputations, and more effective risk management. Furthermore, Lee & Koh (2024) reported that ESG is negatively associated with earnings management, suggesting that stronger governance and oversight mechanisms reduce managerial incentives to manipulate accounting information. These findings indicate that ESG not only improves corporate transparency but also strengthens governance mechanisms that reduce information asymmetry and enhance investor confidence.

ESG is expected to moderate the relationship between earnings management and corporate risk. Although earnings management may increase corporate risk by reducing earnings quality, increasing information asymmetry, and generating negative market signals, companies with stronger ESG disclosure are expected to mitigate these adverse effects through enhanced governance quality, greater transparency, stronger stakeholder accountability, and more credible corporate signals. Consequently, the positive influence of earnings management on corporate risk is expected to become weaker when ESG disclosure is higher. Therefore, the following hypothesis is proposed:

H2: ESG weakens the positive influence of earnings management on corporate risk

3. Methods

3.1 Research Design

This study employs a quantitative research design using secondary panel data. Research data was obtained from banking sector companies listed on the Indonesia Stock Exchange during the 2022-2024 period. This period is the initial phase after the Covid-19 recovery, when the banking sector began to face new dynamics. This study aims to examine the influence of earnings management on corporate risk and the moderating role of ESG. The quantitative approach is considered appropriate because the study aims to empirically test the proposed hypotheses through statistical analysis of numerical data from corporate financial reports, ESG disclosures, and stock prices.

3.2 Population and Sample

The population in this study is all companies listed in the banking sub-sector on the Indonesia Stock Exchange (IDX) during the 2022–2024 period. This period is the initial phase after the Covid-19 recovery, when the banking sector began to face new dynamics. Based on IDX data, there are around 48 banking companies listed on the IDX as of the

end of 2024. The sampling technique used in this study is purposive sampling. The criteria used in this study are: companies are listed in the banking sector on the IDX for the 2022-2024 research period; the company publishes a complete annual report for the 2022, 2023, and 2024 periods; and the company has complete monthly stock price data to calculate stock return volatility during the research period. Based on these criteria, as many as 40 banking companies were identified as a research sample. Because the research period covers three years, namely 2022-2024, the number of observations used in this study is 120 observations (40 companies × 3 years). The purposive sampling approach ensures that the selected sample possesses the characteristics necessary to adequately address the research objectives, particularly regarding the availability of complete financial data, ESG disclosure information, and stock price data for calculating corporate risk.

3.3 Data Collection Techniques

This study uses secondary data obtained from various sources. The annual financial statements of banking companies were published on the IDX website (www.idx.co.id) and on each bank's official website, serving as a source of accounting data for calculating earnings management variables, profitability, and firm size. ESG score data were obtained from sustainability reports and annual reports published by each banking company during the observation period. Historical stock price data, including daily and monthly stock price data, were obtained from the IDX and Yahoo Finance to calculate stock return volatility as a measure of corporate risk. All extracted data were systematically organized into a panel dataset suitable for statistical analysis using the selected analytical software. The secondary data sources employed in this research are considered reliable as they represent official publications from authorized institutions and established data providers.

3.4 Operational Definition and Variable Measurement

Table 1. Operational Definition and Measurement of Variables

Variable	Type	Definition	Measurement	Scale	Source
Corporate Risk (RISK)	Dependent	Totality of future yield uncertainty faced by the company, reflected through stock price volatility	Standard deviation (σ) of monthly stock return	Ratio	Saputra & Triwarti (2026) and Trescova & Firmansyah (2025)
Earnings Management (EM)	Independent	Management actions in regulating reported profits through accounting discretion in credit loss reserve policies	Residual from CKPN estimation model: $LLP_{it} = \alpha_0 + \alpha_1 BNPL_{it} + \alpha_2 CHNPL_{it} + \alpha_3 CHLOAN_{it} + \epsilon_{it}$	Ratio	Kanagaretnam et al. (2004) and Wijaya & Firmansyah (2021)
ESG (ESG)	Moderating	Company's performance in environmental,	(Number of items disclosed / 80 items) ×	Ratio	Putri & Nugraha (2026) and

Variable	Type	Definition	Measurement	Scale	Source
		social, and governance dimensions reflects its commitment to responsible and sustainable business practices	100% (13 governance + 31 environmental + 36 social indicators)		Trescova & Firmansyah (2025)
Profitability (ROA)	Control	The company's ability to generate profits from its total assets	(Net Income / Total Assets) × 100%	Ratio	Trescova & Firmansyah (2025)
Firm Size (SIZE)	Control	The scale of the company's operations is reflected in the economic resources owned and controlled	Ln (Total Assets)	Ratio	Wulandari et al. (2026)

Source: Developed for this research (2026)

3.5 Data Analysis Techniques

Data analysis in this study was conducted using panel data regression, an analytical method that combines cross-sectional and time-series data, and was processed using appropriate statistical software. The analysis procedure consisted of descriptive statistics to characterize the data; panel data model selection using the Chow, Hausman, and Lagrange Multiplier tests; classical assumption tests (including normality, multicollinearity, heteroscedasticity, and autocorrelation); and hypothesis testing using panel data regression. Based on the results of the Chow, Hausman, and Lagrange Multiplier tests, the Fixed Effect Model was selected as the final estimation model. The panel data regression model employed in this study is specified as follows:

$$RISK_{it} = \alpha + \beta_1 EM_{it} + \beta_2 ESG_{it} + \beta_3 (EM_{it} \times ESG_{it}) + \beta_4 ROA_{it} + \beta_5 SIZE_{it} + \varepsilon_{it}$$

Where RISK is corporate risk, EM is earnings management, ESG is Environmental, Social, and Governance, ROA is profitability, SIZE is firm size, α is a constant, β_1 - β_5 are regression coefficients, and ε is the error term. Hypothesis testing employs the t-test for partial effects, the F-test for simultaneous effects, and the coefficient of determination (R^2) to assess model explanatory power, with a significance level of 5% ($p < 0.05$).

4. Results and Discussion

4.1 Descriptive Statistical Analysis

Descriptive statistics are presented to provide a preliminary overview of the research data, including the mean, standard deviation, minimum, and maximum for each variable. Descriptive statistical results for all research variables are shown in Table 2.

Table 2. Descriptive Statistical Analysis Results

Variable	Obs	Mean	Std. Dev	Min	Max
Earnings Management	120	0.0015	0.0323	-0.0591	0.1072
Corporate Risk	120	0.1158	0.1186	0.0075	0.7624
ESG	120	0.6002	0.1766	0.2250	0.9125
ROA	120	0.0132	0.0227	-0.0805	0.1078
Firm Size	120	31.6561	1.6581	28.8290	35.4250

Source: Processed data (2026)

Table 2 presents descriptive statistics for all financial and sustainability variables obtained from 120 observational samples, including corporate risk (RISK), earnings management (EM), ESG disclosure (ESG), return on assets (ROA), and firm size (SIZE). The earnings management variable has an average value of 0.0015 with a standard deviation of 0.0323. The minimum value of -0.0591 and the maximum value of 0.1072 indicate variation in Earnings Management practices, both in reducing and increasing profits. The average value close to zero indicates that, in general, the banking companies in the sample do not exhibit a dominant Earnings Management tendency in any particular direction.

The corporate risk variable has an average value of 0.1158 with a standard deviation of 0.1186. This shows that the level of risk among companies varies widely. A minimum value of 0.0075 indicates a low-risk company, while a maximum value of 0.7624 indicates a relatively high-risk company. The ESG variable has an average value of 0.6002 with a standard deviation of 0.1766. The minimum value of 0.2250 and the maximum value of 0.9125 indicate that the ESG disclosure levels of banking companies are quite diverse. In general, the average value indicates that the companies in the sample have a fairly good level of ESG disclosure.

The ROA variable has an average value of 0.0132 with a standard deviation of 0.0227. A minimum value of -0.0805 indicates a company that has experienced losses, while a maximum value of 0.1078 indicates a company with the highest profitability. Meanwhile, the company's size has an average value of 31.6561 with a standard deviation of 1.6581. The minimum value of 28.8290 and the maximum of 35.4250 indicate that the research sample includes banking companies of various sizes. Overall, the descriptive statistics indicate that the research data have sufficient variation to describe the condition of banking companies in the sample. These variations can be seen from differences in risk levels, earnings management practices, ESG disclosures, profitability, and firm size during the study period.

4.2 Hypothesis Testing

Based on the descriptive statistics described earlier, this study tested the hypothesis using a regression model. This test was conducted to determine the direction and significance of the influence of earnings management, ESG disclosure, earnings management-ESG interactions, firm size, and profitability on corporate risk. The results of the regression test are shown in Table 3.

Table 3. Summary of Hypothesis Testing Results

Variable	Coeff.	t-stat	Prob.
C	0.615	2.94	0.003
EM	-1.325	-1.14	0.254
ESG	0.121	1.73	0.085
EM*ESG	1.578	0.82	0.411

Variable	Coeff.	t-stat	Prob.
SIZE	-0.017	-2.57	0.011
ROA	-0.723	-1.38	0.168
R-square	0.094		
Adjusted R-square	0.055		
F-Stat	2.383		
Prob (F-Stat)	0.042		

Source: Processed data (2026)

Table 3 presents the results of the hypothesis testing. The Earnings Management (EM) variable has a p-value of 0.254, which exceeds the 0.05 significance level, indicating that earnings management has no significant effect on corporate risk. Therefore, the first hypothesis is rejected. Although the coefficient of EM is -1.325, its effect is not statistically significant, suggesting that earnings management practices among the sampled banking firms are not a primary determinant of corporate risk during the observation period. The ESG variable also has no significant effect on corporate risk ($p = 0.085$). Furthermore, the interaction term between Earnings Management and ESG ($EM \times ESG$) has a p-value of 0.411, indicating that ESG does not moderate the relationship between earnings management and corporate risk. Accordingly, the second hypothesis is rejected. These findings suggest that ESG disclosure has not yet served as an effective governance mechanism to mitigate the impact of earnings management on corporate risk. Among the control variables, firm size has a significant negative effect on corporate risk (coefficient = -0.017; $p = 0.011$), indicating that larger firms generally experience lower corporate risk. In contrast, profitability (ROA) has no significant effect on corporate risk ($p = 0.168$).

The overall regression model is statistically significant, as indicated by an F-statistic probability of 0.042, suggesting that the independent, moderating, and control variables jointly explain variations in corporate risk. However, the model yields an R-squared value of 0.094, indicating that only 9.4% of the variation in corporate risk is explained by the variables included in this study, while the remaining 90.6% is attributable to other factors outside the model. These findings suggest that corporate risk in the banking sector is likely influenced by additional determinants, such as macroeconomic conditions, asset quality, credit risk, capital structure, liquidity, and other market-related factors that were not incorporated into the present analysis.

4.3 Discussion

4.3.1 The Effect of Earnings Management on Corporate Risk

The statistical analysis indicates that earnings management has no significant effect on corporate risk; therefore, the first hypothesis is rejected. Based on agency theory, conflicts of interest between managers as agents and company owners as principals can encourage managerial opportunism, including the manipulation of the allowance for impairment losses (CKPN) for earnings-smoothing purposes (Huang et al., 2025). Theoretically, such practices may reduce the quality of financial reporting, increase information asymmetry, and create uncertainty among investors regarding the company's actual financial condition. Under these circumstances, agency theory predicts that earnings management should increase corporate risk because investors face greater difficulty in evaluating the firm's true economic performance.

However, the results of this study indicate that discretionary CKPN is insufficient to influence corporate risk in the Indonesian banking sector during the 2022-2024 period.

This finding can be explained by the characteristics of the banking industry, which operates under strict regulatory oversight. The Financial Services Authority (OJK) requires banks to comply with prudential principles in financial reporting and risk management (Otoritas Jasa Keuangan, 2017). Moreover, the implementation of PSAK 109, which adopts the Expected Credit Loss (ECL) approach, requires banks to recognize allowance for impairment losses based on forward-looking estimates of credit losses, thereby limiting managerial discretion in determining CKPN. Consequently, although managerial judgment remains possible, the scope for opportunistic earnings management is substantially constrained.

From the perspective of signaling theory (Spence, 1973), earnings management is expected to function as a negative signal because it reduces the credibility of financial statements and increases uncertainty regarding a firm's future performance. Nevertheless, the empirical findings suggest that investors in the Indonesian banking sector do not interpret discretionary CKPN as a sufficiently strong negative signal to alter their assessment of corporate risk. Instead, investors appear to place greater emphasis on more observable indicators of bank performance, such as capital adequacy, liquidity, profitability, asset quality, and overall financial stability. Consequently, discretionary CKPN is viewed as a technical accounting estimate rather than a reliable indicator of heightened corporate risk. As long as banks maintain sound financial fundamentals and comply with regulatory requirements, earnings management through CKPN is unlikely to generate substantial market reactions or increase volatility in stock returns.

This finding is consistent with Khoiriyah et al. (2023) and Trescova & Firmansyah (2025), who also reported that earnings management has no significant effect on corporate risk in the Indonesian context. These findings suggest that the market does not always perceive earnings management as a meaningful risk signal, particularly in highly regulated industries where accounting discretion is constrained and closely monitored. Therefore, the insignificant relationship identified in this study may be attributed to the limited discretionary space available under OJK supervision, the implementation of PSAK 109, and investors' greater reliance on broader banking fundamentals than on discretionary loan loss provisions when assessing corporate risk. Consequently, earnings management through CKPN is not sufficiently influential to alter investor perceptions or significantly affect stock return volatility during the 2022-2024 observation period.

4.3.2 The Moderating Role of ESG on the Relationship between Earnings Management and Corporate Risk

The analysis indicates that ESG does not moderate the relationship between earnings management and corporate risk; therefore, the second hypothesis is rejected. Based on agency theory, ESG is expected to function as an effective governance and monitoring mechanism that constrains managerial opportunism, including earnings management. Strong ESG practices should improve transparency, strengthen internal governance, and reduce information asymmetry between managers and investors, thereby weakening the adverse effect of earnings management on corporate risk. Similarly, stakeholder theory suggests that companies with stronger ESG commitments are more likely to maintain the trust of investors, creditors, regulators, and other stakeholders by providing transparent and accountable financial and non-financial information. Consequently, firms with higher ESG performance are expected to experience lower uncertainty and weaker market reactions to earnings management practices.

From the perspective of signaling theory, ESG disclosure serves as a positive signal of a company's governance quality, transparency, and long-term sustainability. Companies with high ESG disclosure are expected to provide investors with greater confidence in the credibility of corporate reporting and the effectiveness of internal control mechanisms. Consequently, positive ESG signals should reduce investor uncertainty and weaken the perceived negative signal of earnings management. However, the finding of this study suggests that ESG disclosure has not yet functioned as a sufficiently credible market signal to mitigate the influence of earnings management on corporate risk in the Indonesian banking sector.

This finding can be explained by the relatively early stage of ESG implementation in Indonesian banking during the 2022-2024 period. ESG disclosures contained in annual reports and sustainability reports may still emphasize regulatory compliance and disclosure completeness rather than substantive improvements in governance quality, internal control effectiveness, and risk management practices. Consequently, although banks disclose ESG-related information, investors may not perceive these disclosures as sufficiently informative to reduce uncertainty arising from earnings management. Furthermore, investors in the banking sector appear to place greater emphasis on more observable financial fundamentals, such as capital adequacy, liquidity, profitability, asset quality, and overall financial performance, when evaluating corporate risk. The relatively limited variation in ESG disclosure among banking firms may also reduce its ability to distinguish firms with genuinely stronger governance and transparency, thereby limiting its moderating role.

This finding is consistent with Khoiriyah et al. (2023) and Trescova & Firmansyah (2025), who reported that ESG has not consistently functioned as an effective governance mechanism capable of altering the relationship between financial reporting practices and corporate outcomes in Indonesia. The results therefore suggest that, although ESG is theoretically expected to strengthen governance, reduce information asymmetry, and provide positive market signals, its implementation and market relevance in the Indonesian banking sector remain insufficient to mitigate the influence of earnings management on corporate risk during the observation period.

5. Conclusion

This study examines the influence of earnings management on corporate risk and the role of ESG as a moderating variable in banking companies listed on the Indonesia Stock Exchange for the 2022-2024 period. Using panel data regression analysis on 40 banking companies with 120 observations, the results show that earnings management does not have a significant effect on corporate risk, indicating that discretionary practices through credit loss reserves (CKPN) in the banking sector are not strong enough to affect investor perception and stock return volatility due to strict regulatory oversight from the Financial Services Authority (OJK) and the implementation of PSAK 109 which limits managerial discretion. ESG has also not been shown to be able to moderate the relationship between earnings management and corporate risk, suggesting that ESG disclosure in the Indonesian banking sector during the post-pandemic period is still in the strengthening stage and has not fully served as an effective supervisory mechanism in mitigating the impact of earnings management on corporate risk. Meanwhile, firm size has a significant negative effect on corporate risk, indicating that larger companies generally have lower risk levels due to greater resources, wider access to financing, and better risk diversification capabilities. Profitability, however, has no significant effect on corporate

risk, suggesting that profitability has not been the main factor explaining variations in corporate risk in this study.

The theoretical implications of this study contribute to the literature on the relationship between earnings management and corporate risk by positioning ESG as a moderating variable. The findings challenge the conventional agency theory assumption that earnings management practices always increase corporate risk, demonstrating that in highly regulated industries such as banking, managerial discretion is limited and does not necessarily translate into market-perceived risk. The non-significant moderating role of ESG suggests that stakeholder theory may have limited applicability in explaining the relationship between ESG disclosure and corporate risk in the Indonesian banking context, as ESG implementation is still in its early stages, and investors may not yet fully consider ESG information in their risk assessment. The significant negative effect of firm size on corporate risk supports the resource-based view, confirming that larger companies possess superior resources and capabilities to withstand external shocks and manage risks effectively.

From a practical perspective, the results of this study indicate that the risk assessment of banking stocks should consider a range of fundamental indicators, not just earnings management information and ESG disclosures. For investors, this study provides insights into how corporate risk in the banking sector is better explained by firm size and other fundamental factors than by earnings management practices or ESG disclosures alone, suggesting a more comprehensive approach to investment decision-making. For bank management, this study provides an understanding of the importance of transparency in financial reporting and credit loss reserve management, grounded in actual economic conditions, as regulatory oversight limits opportunistic discretion. For regulators, particularly the Financial Services Authority (OJK), these results can serve as evaluation material on the effectiveness of ESG implementation and credit loss reserve practices in supporting banking risk management, as well as on strengthening the role of ESG disclosure as an effective supervisory mechanism.

This study has several limitations. First, the observation period only covers 2022-2024, the post-COVID-19 pandemic recovery period, so these conditions may affect corporate risk and earnings management practices in the banking sector and limit the generalizability of the findings to other periods. Second, corporate risk in this study is measured by stock return volatility (TOTRISK), so it does not capture all dimensions of corporate risk, such as credit, operational, or liquidity risk, which may have distinct determinants. Third, ESG measurement is still based on disclosure levels, so it has not fully captured the quality of ESG implementation, as companies may disclose ESG information without substantive implementation. Fourth, the model's low explanatory power ($R^2 = 0.094$) suggests that other significant factors affecting corporate risk were not included in this study. Fifth, the sample is limited to banking companies listed on the Indonesia Stock Exchange, which may limit the generalizability of findings to other sectors or countries.

Future research should broaden the scope by using a longer observation period to capture more comprehensive dynamics and structural changes in the banking sector, and by expanding the scope of study to other sectors or cross-country comparisons to enhance generalizability. It would also be valuable to consider other corporate risk measures beyond stock return volatility, such as credit risk, bankruptcy risk, or systematic risk, to provide a more comprehensive picture of corporate risk determinants. Future research could also use ESG metrics that better reflect implementation quality, such as ESG

performance ratings or third-party assurance, rather than relying solely on disclosure levels. Additionally, incorporating banking-specific variables, such as capital adequacy (CAR), liquidity (LDR), asset quality (NPL), and credit risk, may improve the model's explanatory power and provide deeper insights into the determinants of corporate risk in the banking sector. Finally, exploring the moderating role of other governance mechanisms, such as board diversity, audit committee effectiveness, or institutional ownership, may enrich the theoretical and practical contributions of future studies in this area.

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