Income Diversification, ESG Practices and Financial Sustainability of Listed Non-Financial Firms in Nigeria

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Abstract. Meeting the current financial needs and ensuring resource availability for future operations is vital for firms to maximize their shareholders wealth and improve overall health of the economy. However, ineffective allocation of resources to new ventures and ESG compliance issues have compacted the overall performance thereby undermining the listed non-financial firms' financial sustainability. Consequently, this study investigates the impact of income diversification and ESG practices on the financial sustainability of the firm. Longitudinal research design was used and 84 out of the 104 listed non-financial firms were sampled using multi-stage sampling technique. Data obtained from the annual reports of the sampled firms as well as the ESG-CSR Hub were analyzed using panel data regression (GLS) technique and the findings revealed that income diversification and ESG practices have impact on the financial sustainability of the listed non-financial firms in Nigeria. The study therefore recommends that firms should identify more complementary revenue sources especially in the high-growth sectors in order to minimize investment and operational risk. Also, firms should invest in the energy-efficient technologies and waste management practices while implementing ESG frameworks that will position them competitively in a dynamic environment.

Keywords: Income Diversification, ESG Practices, Financial Sustainability

1. Introduction

Globally, achieving growth, long-term survival and meeting obligations without compromising future operations have been the secondary objectives of firms after achieving the primary motives of profit maximization and shareholders' wealth maximization. Achieving these objectives culminate into financial sustainability of firms thereby enhancing firm's resilience, strengthen sufficient revenue generation to cover costs, enabling firms to navigate economic downturn and withstand external shocks (Sari & Nurwulandari, 2024; Nogueira, et al., 2024). A financially sustainable firm depends less on external financing to invest in new opportunities, has a better access to capital market,

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engages in corporate social responsibility initiatives that will boost competitiveness, investors' confidence while contributing to overall reputation of the firm without compromising profitability (Yunusov, 2024; Anisulowo, et al., 2024)

In Nigeria, the recently introduced economic policies ranging from fuel subsidy removal, monetary reforms, tax reforms, palliatives and inflation control among others have brought financial sustainability to the front burner of listed non-financial firms. Before now, the motive to achieve operational stability, access to capital market, reputation and stakeholder trust, market competitiveness has been the driving force as listed non-financial firms strive in meeting the obligations to shareholders, employees and creditors while continuing to invest in growth opportunities (Nwadialor & Nweze, 2020; Umar et al., 2022). However, the current economic instability, high operating costs, regulatory challenges, market competitions pose hazardous threats to the financial sustainability of listed non-financial firms. The fluctuation of currency value and inflation rates of over 22% has led to increased operational costs, eroded the consumers' purchasing power thereby making it challenging for firms to maintain stable profit margin and cash inflows (Idisi, et al., 2023; Dagunduro, et al., 2024; Bamidele, 2024).

Essentially, one major means of achieving financial sustainability is income diversification. By diversifying income sources, the prime risk attributable to single-revenue stream is eliminated as firms get buffered against economic downturn or industry shocks, less vulnerable to market fluctuations, make the firms' asset portfolio more attractive while achieving competitive advantage (Umar et al., 2022; Abubakar, 2024). Despite these benefits of income diversification to firms, the Nigerian listed non-financial firms are yet to optimize it as they are faced with challenges of resource allocation, market familiarity and expertise, strategic focus and core competence dilution, operational complexity market knowledge gaps or saturation among others (Nwadialor & Nweze, 2020; Umar et al., 2023). The firms' financial sustainability is undermined owing to losses from strategic missteps due to the insufficient understanding of market dynamics (Abubakar, 2024).

Furthermore, a major integral part of financial sustainability of firms is the adoption and implementation of Environmental, Social, and Governance (ESG) practices as more investors particularly the institutional investors who primely prioritize sustainability get attracted to the firms with a robust ESG practices (Ubandawaki, 2024). While waste reduction and less energy consumption form the environmentally sustainable practices, socially responsible practices involve employee's satisfaction, productivity enhancement, fair labour practices and community engagements which indirectly minimize risks associated with regulatory penalties and reputational damage and ultimately supports financial performance (Duho, et al., 2020; Uwalomwa et al., 2021; Ajayi, 2024). However, lack of awareness and understanding, high implementation costs,

data availability and quality, cultural resistance and limited stakeholder engagement still constitute the challenges of ESG practices in achieving financial sustainability of Nigerian listed non-financial firms. The regulating framework for ESG in Nigeria is still evolving thereby hindering firms' full commitment to ESG initiatives thinking that the compliance costs outweigh the benefits (Bamidele, 2024; Dagunduro, et al., 2024).

From the foregoing, it becomes imperative to pontificate the prime impact of income diversification as well as the ESG practices in entrenching the financial sustainability of Nigerian listed non-financial firms.

2. Literature Review

2.1 Conceptual Review

Financial Sustainability

Financial sustainability refers to an organization's ability to bring in enough money to pay for its operations, make growth investments, and weather economic fluctuations; in other words, it entails using sound financial management techniques that support long-term objectives (Gleißner, et al., 2022). Mhlanga, (2024) asserted that financial sustainability involves joining social and environmental considerations with the financial success as all-inclusive strategy pontificate the connection between responsible resource usage, stakeholders' participation and financial stability which are broader sustainability objectives. Financial sustainability as labelled by Zabolotnyy and Wasilewski (2019) is a preservative means of long-term financial health by ensuring that the organizational goals or ability to provide services are not jeopardized while sustaining the ongoing or future operations. This emphasizes how crucial strategy and planning are to establishing sustainable financial habits.

Furthermore, financial sustainability is perceived to be all encompassing as it is a resultant effect of economic sustainability, environmental sustainability, social sustainability, operational sustainability, investment sustainability, financial resilience etc. (Ur Rahman, et al., 2020; Tipu, 2022; Mhlanga, 2024). Practically, the features of financial sustainability among other things include robust financial management, income diversification, adoption of ESG principles, financial resilience, stakeholder involvement, investment in innovation, and transparent reporting. Together, these components support businesses' long-term viability and success in a challenging economy (Nwadialor & Nweze, 2020; Gleißner, et al., 2022)

Income Diversification

Income diversification is defined as the process or strategy of generating income from multiple investments or activities instead of relying on a singular source in order to mitigate risks attributed to economic downturn or market fluctuations (Gupta & Kumar, 2023; Oyetunde & Oyetunde, 2022). With respect to an investment perspective, income diversification can be described as an activity of dispersing investment across dissimilar asset classes ranging from real estate, bonds or stocks in order to heighten returns and curtail risks. This strategy gives the investors the ability to achieve more stable financial results over time while balancing their portfolios (Mac-Ozigbo & Daniel, 2020; Bhutto, et al., 2020). According to Lichtenstein (2020), income diversification involves generating revenue via diverse geographical market or partaking in numerous business lines to lessen single-source dependency and ensure consistent cashflow.

Okeke & Nwude (2022) asserted that income diversification is a strategic approach that exhibit certain features such as expansion into non-core activities, product and service diversification, risk mitigation, increased competitiveness among others. With income diversification, firms are able to own new customer base and tap into new markets thereby leading to cross-subsidization as profit from one line of business can be used to augment other lines of business (Ur Rahman, et al., 2020). Also, in the efforts of being financially resilient, firms have multiple revenue streams to the extent of investing in financial assets like equities or bonds that gives dividend, interests, or capital appreciation thereby making firms withstand market volatility (Idisi, et al., 2023)

ESG Practices

Environmental, Social, and Governance (ESG) practices are an assortment of guidelines that assess how a business operates and how sustainable it is over the long run based on how it treats stakeholders, affects the environment, and its governance structure. ESG practices have gained prominence because investors and stakeholders are running businesses not only for moral leadership and social responsibilities but also to solve sustainability challenges (Serafeim & Yoon, 2022). The main impact of the company’s operation on the environment is enshrined in the environmental component of ESG as it entails usage of renewable energy sources, reduction of carbon emissions, waste minimization and reducing resource depletion. Companies that give priorities to the environmental sustainability aims to attain parity between ecological conservation and profitability. (Friede, et al., 2015; Shahbaz et al., 2021).

Furthermore, a company's management of connections with suppliers, customers, workers, and the communities in which it operates is assessed as part of the social

dimension of ESG. It addresses issues ranging from community involvement, diversity and inclusion, human rights, and labour standards. Robust social policies cultivate faith and allegiance among interested parties, augmenting a business's standing and clientele (Giese & Nagy, 2021). Governance includes the leadership structure of the organization, ethics, transparency, and adherence to legal and regulatory requirements. In addition to preserving shareholder interests and ensuring accountability, good governance also reduces the likelihood of corporate scandals. Businesses that place a high priority on good governance typically outperform competitors over time because they face less risks from unethical behaviour and penalties from the government (Gillan et al., 2021).

2.2 Theoretical Framework

Resource Based Theory (RBT)

The Resource Based Theory (RBT), sometimes referred to as the Resource Based View (RBV), remains a paradigm for policy/strategic management which is based upon the idea that a company's distinct skills and resources are what provide it a competitive edge and long-term financial stability. For these resources to offer long-term competitive advantages, they must be valuable, rare, inimitable, and non-substitutable (VRIN framework) (Barney, 1991; Peteraf, 1993). According to RBT, businesses that better utilize their unique resources would be able to control expenses, provide steady revenue streams, and beat rivals over the long term in the context of financial sustainability (Teece, et al., 1997; Grant, 1991). This postulation is braced by income diversification, which permits firms to utilize their current resources such as technological capital, financial capital or human capital across a variety of commercial ventures thereby lessen their dependency on a single revenue source, taking advantage of synergies as well as improving their continuing financial sustainability. Income diversification is a common strategy used by listed non-financial companies to optimize the application of their core strengths across many business lines, potentially resulting in increased profitability and long-term growth (Olugbenga et al., 2021).

2.3 Empirical Review and Hypotheses Development

Income Diversification and Financial Sustainability

Many studies have been conducted on income diversification, but because they focus primarily on a single industry thereby having the results and justifications vary. On one hand, empirical research has shown that firms with a variety of revenue streams are generally better able to withstand economic downturns, have higher profitability, have stable cash flows, are resilient geographically, draw in industry-specific advantages, are flexible in their approach, reduce over-dependency, and anticipate long-term growth opportunities. Additionally, empirical research showed that Nigerian manufacturing

companies that expanded into related industries recorded higher levels of financial stability than those in less flexible businesses like oil and gas because they were able to better use their resources and operate more efficiently (Sulimany, et al., 2021; Nguyen & Le, 2021; Ozturk and Demir, 2019; Karanja et al., 2022; Choi & Wang, 2020; Chong & Lee, 2020; García-Herrero & Gavila, 2019; Li et al., 2020; Ani & Ugwuanyi, 2023). On the contrary, the inefficiencies that may emanate from over-diversification risk are main protestations to income diversification in achieving financial sustainability. The financial performance and sustainability of the firm may be lowered due to inefficient resource allocation which may tilt businesses to excessively spend in unrelated new projects at the expense of their fundamental business operations. Another area of assessment is from shareholders' viewpoint as some shareholders may negatively respond if they believe that diversification strategies fail to align the companies' strategic objectives or too risky and this would have impact on the firm's financial sustainability (Lin & Jin, 2019; Duho, et al., 2020; Olalere, et al., 2021; Choi & Wang, 2020; Uwalomwa et al., 2021; Berger & Ofek, 2020).

H_{01}: Income diversification does not significantly impact the financial sustainability of Nigerian listed non-financial firms.

ESG Practices and Financial Sustainability

Empirical studies portray that ESG practices proffer an array of benefits to firms ranging from risk mitigation, cost reduction, enhanced reputation and brand value, attracting and retaining talents, long-term value creation, improved financial performance, stakeholder engagement and trust as well as investment resilience in crises. Having operational disruptions, legal liabilities and reputational damage due to ecological issues, social concerns and governance/institutional matters create a likelihood of financial losses thereby threatening the financial sustainability of the firms (Aouadi, et al., 2020; Giese & Nagy, 2021; Broadstock, et al., 2021; Fatemi et al., 2020; Dyck et al., 2019; Sassen et al., 2019; Laskar, et al., 2017; Zhang, et al., 2020; Alareeni, et al., 2020). Conversely, critics argued that ESG practices in firms creates short-term profitability sacrifices, higher compliance and reporting costs, dilution of shareholder value, greenwashing and misleading claims, market and investor skepticism of overregulation, conflicting stakeholder interests and overemphasis on non-financial metrics. Company's resources especially the smaller firms tend to be strained while implementing sustainable technologies that strictly adhere to stringent environmental and social regulations. This arguably dilutes shareholders value as other stakeholders such as communities, clienteles or employees are prioritized above the shareholders. (Berg, et al., 2020; Bradley & Bothello, 2020; (Amel-Zadeh & Serafeim, 2018; Pedersen, et al., 2021; Giese & Nagy, 2021; Chritstensen, et al., 2019; Botosan, 2020; Liakh, 2022; Chen, et al., 2023).

H_{02}: ESG practices do not significantly impact the financial sustainability of listed Nigerian non-financial firms in Nigeria.

3. Methodology

This study utilizes longitudinal research design purposely to study the changes over time as well as observe developments and long-term effects of income diversification and ESG practices on the financial sustainability of Nigerian listed non-financial firms. The population comprises the 104 listed non-financial firms in Nigerian. Krejcie and Morgan's (1970) was used to sample 84 listed non-financial firms while utilizing multi-stage sampling technique to promote representativeness among all the 10 sectors constituting Nigerian non-financial firms. For a period of 2018 to 2023, data for income diversification and financial sustainability was sourced from the financial statement of the sampled firm while the information for ESG practices was obtained from ESG-CSR Hub which is a reliable source for data relating to ESG.

3.1 Model Specification

To achieve the main thrust of this study which is to investigate the impact of income diversification and ESG practices on the financial sustainability of Nigerian listed non-financial firms, this study modified the model of Alshareef (2024) on financial sustainability of Saudi listed firms.

To achieve the objective of this study, the model was adapted as:

$$FS = \beta_0 + \beta_1 INC_{it} + \beta_2 ESG_{it} + \beta_3 SIZE_{it} + \beta_4 LEV_{it} + \mu_{it} \quad (1)$$

Where:

FS = Financial Sustainability

INC = Income Diversification

ESG = ESG Practices

SIZE = Firm Size

LEV = Leverage

μ = Error Terms

Table 1: Variable Measurement

Variable	Construct	Measurement	Source
Dependent Variable			

Financial Sustainability (FS)	SGR (%)	PM∗ AT ∗ FL ∗ ERR	Alshareef (2024).
Independent Variables			
Income Diversification (INC)	Herfindahl Hirschmann concentration Index	$HHI = \sum_{i=1}^{N} (\frac{Revenue_i}{Total\ Reven}$	Ammar & Boughrara, 2019;
ESG Practice (ESG)	ESG Rating	Overall ESG rating and E,S,G score	
Control Variables			
Firm Size (SIZE)		Ln total Asset	Nurhandari & Choiriyah, 2023
Leverage (LEV)		Total Debt/Total Assets	Gungoraydinoglu & Öztekin (2021).

SGR (%) = PM∗ AT ∗ FL ∗ ERR
where SGR = sustainable growth rate, PM = profit margin (net income after tax/revenue), AT = assets turnover (revenue/total assets), FL = financial leverage (total debt/total assets) and ERR = earnings retention rate (retained earnings/net income after tax).

4. Results and Discussion

4.1 Descriptive Statistics

Table 2: Summary Statistics

Variable	Obs.	Mean	Std. dev.	Min	Max
Fs	504	61.8869	14.81446	37	87
Inc	504	0.45996	0.219002	0.231579	1.1
Esg	504	47.4623	9.662627	31	64
Size	504	23.61798	1.870427	17.86358	27.40453
Lev	504	1.895172	2.870573	0.022951 9	34.14255

Source: Authors' computation (2024)

Table 2 above shows the mean, standard deviation, minimum and maximum values for financial sustainability, income diversification, ESG practices, firm size and leverage. It was found out that the mean value of the financial sustainability is 61.89% and standard deviation of 14.81, it means that there is some dispersion of the data but on average, most of the data are closely related to the mean. The range is from 37% to 87%, which shows that a bunch number of firms are below the mean value. In addition, the income diversification is statistically defined by its minimum and maximum values of 0.231 and 1.1 with the mean value of 0.46 and standard deviation of 0.219. Implicitly, the dispersion is much narrower as the standard deviation is less than the mean values. Furthermore, the research findings showed that ESG practices mean was 47.46, standard deviation of 9.66, minimum value of 31 and maximum of 64. This pontificate the distribution of ESG scores between the sampled firms indicating that the ESG rating is at a moderate level for the firms.

Moreso, the control variable of size has the minimum value of 17.86 and the maximum value of 27.4, and the mean value of 23.62, with the standard deviation of 1.87. This tend to suggest that the sampled firms are relatively large as there was a little deviation from the mean. The second control variable, leverage, was established as M = 1.8951; SD = 2.8705; min = 0.0229; max = 34.142. This means that while there is moderate level of financial leverage among the firms, then are quite balanced off or relatively close to the mean.

4.2 Normality Test

Table 3: Shapiro–Wilk

Variable	Obs	W	V	z	Prob>z
fs	504	0.96192	12.902	6.15	0.0743
inc	504	0.86876	44.465	9.125	0.0685
esg	504	0.97331	9.043	5.295	0.0758
size	504	0.96006	13.532	6.264	0.0698
lev	504	0.47027	179.481	12.481	0.8723

Source: Authors' computation (2024)

Table 3 reveal the normality test result of the variables using Shapiro-Wilk test. The variables financial sustainability, income diversification, ESG practices, leverage and size have p-values of 0.0743, 0.0685, 0.0758, 0.0698 and 0.8723 respectively. This suggests

that the data do not significantly deviate from a normal distribution and are therefore considered to be normally distributed.

4.3 Correlation Matrix

Table 4: Pairwise correlation

	fs	inc	esg	size	lev	VIF	1/VIF
fs	1.0000					-	-
inc	0.0494	1.0000				1.00	0.996366
esg	0.1034	-0.059	1.0000			1.01	0.986522
size	0.0301	-0.0036	-0.0982	1.0000		1.01	0.986512
lev	-0.1441	0.0091	-0.0246	0.0636	1.0000	1.00	0.995546
Mean VIF						1.01	

Source: Authors' computation (2024)

Table 4 presents the correlation analysis between the regressand (financial sustainability) and the regressors (income diversification, ESG practices, firm's size and leverage). The result shows that low and positive relationship exist between income diversification, ESG practices, size and financial sustainability with correlation coefficient of 0.0494, 0.1034 and 0.0301 respectively. Conversely, the leverage has negative relationship with the financial sustainability of the firms with correlation coefficients of -0.1441. In addition, the multicollinearity test was conducted using the variance inflation factor to detect any unstable estimates of regression coefficient that may weaken the model's ability to predict or explain the dependent variable. The result as presented in the Table 3 shows that there was no multicollinearity among the regressors which supports the reliability of the regression coefficients for these variables.

4.4 Generalized Lease Square Regression results

Table 5: Hausman result

	---- Coefficients ----			
	(b)	(B)	(b-B)	sqrt(diag(V_b-V_B))
	fe	Re	Diffference	Std. err.
inc	2.879436	2.873396	0.00604	0.3953876
esg	0.1492584	0.1476586	0.0015998	0.0067812
siz	0.1000859	0.0939106	0.0061753	0.0246924
lev	-0.7460132	-0.725728	-0.0202852	0.0227237

Prob > chi2 = 0.9171

Source: Authors' computation (2024)

Table 5 above presents the hausman result which is to evaluate the consistency of the estimator as well as select the suitable model between the fixed-effect and the random effect. The p-value of 0.9171 indicated the rejection of the alternative hypothesis thereby making the random-effects model more appropriate for this data set.

Table 6: Random-effects GLS regression

FS	Coef.	St. Err.	t-value	p-value	Sig
INC	2.873	0.68	4.19	.001	***
ESG	.148	.068	2.17	.03	**
SIZE	-.094	.351	-0.27	.789	
LEV	.726	.228	3.19	.001	***
Constant	59.794	9.339	6.40	0	***

Mean dependent var	61.887	SD dependent var	14.814
Overall r-squared	0.033	Number of obs	504
Chi-square	16.860	Prob > chi2	0.002
R-squared within	0.034	R-squared between	0.082

*** *p<.01, ** p<.05, * p<.1*

Source: Authors' computation (2024)

Table 6 present the regression results of the random-effect model and it can be deduced that the overall r-squared is 0.0327 indicating that the variable captured (income diversification and ESG practices) only account for small proportion (3.27%) of the variation in the financial sustainability of the listed non-financial firms in Nigeria. Moreso, the wald chi-squared result of 16.87, with the p=value of 0.021 pointed out that the specification of the income diversification, ESG practices as a group was statistically significant for the financial sustainability. Income diversification has a coefficient of 2.873 meaning that a direct change in the income diversification will result to 2.87 change in the aspect of financial sustainability. Further, the p-value of income diversification is 0.001 thereby leading to the acceptance of the alternative hypothesis which states that the income diversification significantly impacts the financial sustainability of the listed non-financial firms in Nigeria.

Furthermore, the ESG practices has a coefficient of 0.147 and the p-value of 0.03 implying that a unit change in ESG practices will lead to 0.147 change in the financial sustainability of the listed non-financial firms in Nigeria. The significance of the p-value leads to the rejections of the null hypotheses and acceptance of the alternative hypothesis implying that ESG practices do have a significant effect on the financial sustainability of the non-financial firms that are listed in Nigeria. However, the coefficient for size as the control variable is positive and is statistically significant to the financial sustainability of the listed non-financial firms in Nigeria but firm's leverage entails a negative correlation with financial sustainability and it is yet insignificant.

4.5 Discussion of Findings

Based on the result presented in Table 6, it can be deduced that income diversification and ESG practices positively and significantly impact on the financial sustainability of the listed non-financial firms in Nigeria. By implication, firms with a diversified revenue source tends to achieve consistent and stable cash inflow through a sustained operation that will make them less vulnerable to financial risk, show better resilience during economic downturn and enhance investment potential. A prominent implication of income diversification is the risk mitigation as a diversified firms are not only positioned to offset industry-specific risk by leveraging on income from unrelated sources, but also take advantage of negative correlation of the investment in their portfolio thereby reducing the overall risk of the company. This finding alludes to the postulation of the resource-based theory that a company that utilizes different resources at its disposal tend to depend less on a single revenue source thereby leading to financial sustainability. This finding aligns with Ani & Ugwuanyi, (2023) Chong & Lee, (2020) and Choi & Wang, (2020)

In addition, the qualitative impact of ESG practices on firms is highly tremendous as firms that comply with ESG practices tend to enjoy customer loyalty with a strengthened brand, cost saving, operational efficiency, competitive advantage, long-term value creation, improved regulatory compliance, less penalties, operational resilience among others. These qualitative impacts tend to influence the consumer/customer's landscape which ultimately result to financial advantage for ESG compliant firms. This finding aligns with the resource-based theory as firms that indulge in ESG practices into their core strategies tend to foster unique resources that will not only support financial performance but also promote financial sustainability of firms. This finding aligns with Laskar, et al., (2019); Broadstock, et al., (2021); Fatemi et al., (2020).

5. Conclusion and Recommendation

Based on the findings of this study, it is evident that income diversification and ESG practices play a significant role on the financial sustainability of listed non-financial firms

in Nigeria as effective income diversification improve the financial resilience of the firms while ESG practices create a better positioning for firms and consequently boost the company brand investors' confidence. It is therefore recommended that firms should identify more complementary revenue sources especially in the high-growth sectors in order to minimize investment and operational risk. Also, giving the rising costs and resource constraints in Nigeria, listed non-financial firms should invest in the energy-efficient technologies, water conservation and waste management practices while implementing ESG frameworks that will position them competitively in a dynamic environment.

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