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Capital market perspectives on sustainability accounting and reporting.

Richard Slack, Durham University Business School

Abstract

There has been a volumetric increase in sustainability reporting information over the last 30 years coupled with the advent of reporting frameworks and reflective of global awareness of sustainability issues. This chapter reports on those qualitative-based studies that have examined, over that period, the (perceived) decision-usefulness of sustainability reporting to capital market users comprising equity and debt financing perspectives. Research methods have predominantly employed survey/questionnaire and experimental studies and since 2000, the growth in interview-based studies. Whilst recognising increased investor awareness of sustainability related issues over time from initial ignorance, clear tensions are consistently reported concerning its decision-usefulness. Primarily these encompass the prevalence of financial measurement and the associated focus on the economic impact of sustainability issues, and criticisms regarding reporting balance, consistency and comparability. The chapter reflects on investor led demand that may help redress these tensions and the need for the wider appreciation of the significance of sustainability beyond its financial impact. The current international developments surrounding sustainability reporting are highlighted as well as offering suggestions for future research.

Key words

Sustainability, decision-usefulness; investors; equity; debt

1. Introduction

There has been a volumetric and accelerating increase in sustainability reporting by companies either through annual report information or stand-alone sustainability reports and hence the availability of such information to capital market users in equity and debt markets. For instance, the World Resources Institute (2019) highlighted that in 2017, 85% of S&P 500 Index companies published sustainability reports (20% in 2011) and 74% of the world's 200 largest companies used the GRI Standards for sustainability reporting (and see Grewel et al. 2021). Moreover, and of direct relevance to this chapter, Principles of Responsible Investment (PRI) (2021) report 3,038 signatories as of 31 March 2020 representing investment assets of US $103.4trn. Further, McKinsey (2019, p.5) reported findings from the Global Sustainable Investment Alliance that global assets managed according to sustainable-investment strategies more than doubled from 2012 to 2018, rising from $13.3trn. to $30.7trn.

Against such a context, this chapter reports on those studies that have examined the views of capital market participants with regard to sustainability reporting, and specifically its decision-usefulness to them. The scope of this chapter is focused on those studies that have adopted a qualitative approach through direct participant-based research covering interview, survey, experimental and questionnaire-based studies with equity retail and institutional investors/fund managers, private investors, sell-side and credit analysts and providers of debt finance and not market-based archival studies that do not directly capture participant views. On participant-based research, Georgiou (2018, p. 1301) comments that his interviews with investors enabled him to "get perceptions, observations, and thoughts" and such a setting provides an interface to "real users in real markets" (Power, 2010, p. 208).

The chapter is structured as follows: Section 2 outlines the meaning and framing of sustainability reporting and the inherent broad and diverse nature of such reporting, being an important consideration for Sections 3 and 4. Section 3 examines the substantial literature on equity investor opinion and is divided into four subsections. Sections 3.1 to 3.3 present the developments and related issues in sustainability reporting over three time periods and reports the views of equity investors regarding its decision-usefulness to them. Reflections on the research methods employed and the related findings over those periods are provided in Section 3.4. Section 4 covers debt market views, and Section 5 presents contemporary investor opinion on sustainability reporting and current developments as well as suggestions for future research.

2. Meaning and framing of Sustainability Reporting

The framing of sustainability reporting is initially reviewed to contextualise the chapter and the strands of research that will be examined in subsequent sections. Historically, The Brundtland Report (1987) ('Our Common Future') issued by The United Nations World Commission for the Environment and Development (UNWCED) is recognised as moving sustainability from ecology to a broader social and policy agenda (see Bebbington and Larrinaga, 2014). The Commission defined sustainable development as development that "meets the needs of the present without compromising the ability of future generations to meet their own needs" (UNWCED, 1987, p. 8). Enmeshed within sustainability are the three pillars of economic growth, environmental protection and social equality giving rise to Triple Bottom Line Reporting (Tilt, 2007). Hence, as argued by Lamberton (2005, p. 19) in his review of sustainability reporting, such accounting information "must exhibit the qualitative attributes of transparency and comparability in a relevant sustainability context to enable stakeholders to assess the environmental and social impact of the organization". Indeed, "Sustainability reporting is the practice by which they [companies] disclose their significant *economic, social and environmental* impacts. This information is critical to inform decisions for a wide range of stakeholders, ranging from employees to policy makers and from customers to *investors* (GRI, 2020, p.1)" (emphasis added) (Adams and Abhayawansa, (2021, p. 8).

However, reflective of the broad nature of sustainability, a range of 'working definitions' in academic research have emerged for its reporting. For instance, Rowbottom and Lymer, (2009, p. 176) refer to sustainability as the information provided by companies on the wider economic, environmental, social and ethical impacts of their activities. Byrch et al. (2015, p. 671) refer to the "plurality of understanding surrounding sustainability" being inherently contested, complex and subjective such that "sustainability is most commonly described as pragmatic and action-oriented − a "middle way" combining economic, social, and environmental concerns as a triple bottom line" (p. 692). Similarly, ACCA, (2016, p. 8) report that "there is no standard, universally agreed definition of the term but, for the purposes of this report, sustainability reporting is defined as information that communicates how flows of material, resources and services between corporations, capital markets, society, the economy and the environment affect the ability of corporate, economic, social and environmental systems to continue and flourish". Further, Stubbs and Higgins (2018, p. 491) note that sustainability reporting research "encompasses social and environmental accounting (SEA), corporate social responsibility (CSR) reporting, triple bottom line (TBL) reporting and sustainability reporting" as well as the commonly referred to environmental, social and

governance (ESG). Indeed, Stubbs and Higgins (2018) use the term 'sustainability reporting' to cover these various strands of research. More generally, in their respective literature reviews on CSR and non-financial reporting, Hinze and Sump (2019) and Michelon et al. (2020) both highlight that CSR and sustainability are used interchangeably within the literature and practice. Following this, the chapter covers the corresponding range of research under the sustainability reporting 'umbrella' on the views of capital market participants.

Whilst sustainability reporting in its various forms has attempted to address the increasing demands for non-financial reporting through increased disclosure of environmental and social performance (Simnett and Huggins, 2015), Bebbington and Thomson (1996), report a weak understanding of sustainability with an overriding emphasis on economic growth. Byrch et al. (2007) report that the meaning of sustainable development presented by business representatives emphasises the economic domain and the notion that a healthy economy with strong development and growth precedes environmental and social improvement and well-being. Further, Barkemeyer et al. (2014, p. 243) report "companies have been found to use a plethora of definitions for various sustainability indicators as well as varying reporting scopes and boundaries often leaving out essential information about sustainability performance".

Mindful of the plurality of sustainability as well as the multiple reporting frameworks that have been developed since the Brundtland Report, Slack and Tsalavoutas (2018, p. 194) in their research with equity market fund managers and analysts, highlight this diversity and the associated acronyms as potential barriers to its wider use and usefulness. They report on one of their respondents on their understanding of ESG type information "I mean this whole industry is very jargonistic, the whole sort of 'ESG', "SRI" – there you go, the jargon itself, it's full of acronyms which if you're trying to turn it mainstream just doesn't help". More generally Pinney et al. (2019, p. 86) note that "the primary challenge [to investor use] continues to be the lack of a normative and widely accepted definition of ESG and standards for companies when measuring and reporting on ESG performance", an issue that is returned to in Section 5. The substantial body of sustainability-related research with equity market participants is now presented.

3. Sustainability reporting: Equity market perspectives

Whilst there is a considerable body of market-based archival and empirical literature examining the value relevance of sustainability reporting (and see Hinze and Sump 2019 for a literature review detailing such studies), there is also a substantial history of participant-based

research engaging with equity market participants, predominantly with fund managers and sell-side equity analysts. Historically and remaining relevant today, Tilt (2007, p. 104) noted the "primary or economic stakeholders are providers of finance and, the focus of much research is in relation to shareholders as providers of equity finance and the equity market comprised fund managers and analysts". Eccles and Serafeim (2013) highlight the criticality of integrating sustainability issues into strategy and that "such a strategy requires the support of the company's investors especially those who might otherwise be inclined to put pressure on the company to focus on quarterly earnings" (p. 9). Further, on sell-side analysts, Hinze and Sump (2019, p. 127) recognise their importance as "key information intermediaries in capital markets and therefore represent a group of capital market participants of major interest…They shape investor judgements and influence their decisions" (and see Campbell and Slack, 2008; 2011; Drake et al., 2019).

Given the exponential growth in sustainable equity investment and the emergence of reporting frameworks since the Brundtland report and more specifically from the Global Reporting Initiative (GRI) guidelines first issued in 2000, it is apposite to review the early, and seminal literature in this area to contrast the key findings with subsequent and more contemporary research. Notably, Tilt (2007, p. 115) remarks "while recognizing that social and environmental issues are important and necessary considerations for organizations, [investors] still give precedence to financial issues and require only information about things that have direct financial impact". Specifically, this chapter helps consider whether there has been a shift in investor sentiment towards their use and the usefulness of sustainability reporting information to them whilst highlighting their associated criticisms of such reporting over time.

3.1 'Early' social and environmental literature with equity market participants

In the early literature, that prior to 2000, the key issues examined were the decision-usefulness specifically of social and environmental disclosures in the annual report. In general, the research commonly employed experimental or questionnaire-based methods with fund managers or analysts receiving annual report financial information with additional social or environment reporting information as appropriate for equity investment decisions. Overall, the findings from these early studies predominantly showed a lack of interest in ESG/sustainability issues, viewed by investors as not relevant or only of relevance through a direct adverse financial consequence.

In very early work, Buzby and Falk (1978) surveyed mutual fund directors to

determine if social information was considered in their investment decision-making. Although the respondents indicated that some social information was useful, eight of the nine categories of social information were not considered to be as important as six selected financial items, with a focus on financial information and performance in equity decision-making. Harte et al. (1991), based on a questionnaire survey, focused on 14 ethical unit trusts, with responses from 11 of those surveyed, found that the environmental record and awareness was the top scoring disclosure attribute of related SEE information, "yet seem to be ill served by the annual report and accounts" (p. 239). Teoh and Shiu (1990) reported the results of a survey with 38 (from an initial sample of 200) Australian investment analysts and managers. Whilst social responsibility information (SRI) was taken into account by them, it was not the driver of decision-making, with their prime focus on financial performance. Further, disclosure of SRI was perceived as too general and vague and was described by one respondent as "decorated items" (p. 75). Hence, "if SRI could be presented in quantitative and financial form, such disclosure would have been perceived as more important for the investment decisions of institutional investors" (p. 75). These issues of 'decoration', and poor environmental performance reporting are issues that remain and are further developed in the later literature. Moreover, in a study of the attitudes of British investment analysts on issues pertaining to the environment, Business in the Environment (BiE, 1994, p. 31) found that environmental issues rank very lowly in the analysts' priorities when they undertake their investment analysis such that "the majority of analysts believed environmental considerations were simply not relevant to them.

In the late 1990's, the seminal experimental studies of Milne and Chan and Deegan and Rankin laid the foundations for a stream of subsequent research examining the decision-usefulness and investment related decision-making of more general social and environmental disclosure. Firstly, the two studies by Milne and Chan. Milne and Chan (1999) using a sample of annual report users (comprised 50 accountants and investment analysts) found that social disclosures from annual reports did not elicit any more than a 15% switch in investment funds. Indeed, they concluded that analysts "largely ignore narrative social disclosures for their investment decision making…[with] disclosures having little effect on investment decisions" (p. 452). Chan and Milne (1999) report on an experimental survey with 54 investors and accountants in New Zealand on the decision usefulness of disclosures on firms' environmental performance, using cases of 'good' and 'bad' environmental performance and specifically how investors allocate their investment funds. With regard to positive environmental disclosures, they found no investor reaction, but conversely for

negative disclosures, "the dominant behaviour was one of avoidance on the grounds of increased exposure to environmental liabilities and future expenditures" (p. 274). Hence, their concern in relation to the financial consequences of environmental performance and disclosure, rather than any social or moral issue per se, and their observation that, given this, firms will rarely voluntary disclose negative environmental information, giving rise to impression management and green-washing which are prevalent aspects of subsequent literature in the area (see especially Section 3.3).

Secondly, the two Australian user-based questionnaire studies of Deegan and Rankin (1997; 1999), examining environmental reporting. Deegan and Rankin (1997) found that whilst environmental information was important to some user groups (notably non-institutional investors 72%) it was of little importance to stockbrokers and investment analysts (43%) and for both groups financial information and performance was more material. Further, that annual report disclosures relating to the environmental performance tend, on average, to be biased and self-laudatory with minimal disclosure of negative environmental information, a finding consistent with the implications raised by Chan and Milne and consistent with Deegan and Gordon (1996) and Deegan and Rankin (1996) on the significant lack of negative environmental disclosure compared to the emphasis on reporting positive news. Despite these criticisms, even where environmental disclosure is demanded, Deegan and Rankin (1999) reported that only 24% of preparers supplied such information with the majority having no plans to do so due their perceived (or real) lack of importance to users.

Reflective of such findings in the early literature and the marginalised view of social and environmental disclosure compared to financial performance and reporting, and as a precursor to Sections 3.2 and 3.3, Gray (2006, p. 79) laments, "taken in the round, the evidence seems to be that currently, while investors can *recognise* and respond to the *economic implications* of social disclosure, the *value-relevance of disclosure is often perceived as marginal*" (emphasis added).

3.2 Advent of reporting frameworks and investor networks 2000 to 2010.

Post 2000, saw the publication of GRI guidelines relevant to sustainability reporting and the conception of The Millennium Development Goals with its focus on, inter alia, global poverty, education, equality and environmental sustainability, the latter covered by Goal 7[1].

[1] See https://www.un.org/millenniumgoals/environ.shtml

Accounting for Sustainability (A4S) was launched in 2004 to develop decision-making and reporting systems that take into account the longer-term and broader consequences of actions and responding to the sustainability challenges faced in the 21st century.

From an investor perspective, the Enhanced Analytics Initiative was established in 2004 designed to encourage sell-side research beyond short term financial data and to recognise the importance of social and environmental, as well as financial, performance. The Social Investment Forum (SIF) and the Principles for Responsible Investment (PRI) initiative as international networks of investors were launched in 2006. Specifically, PRI aims to understand the implications of sustainability for investors and to support signatories to incorporate these issues into their investment decision making and ownership practices and seek relevant ESG disclosures by companies. Indeed, Hockerts and Moir (2004) analysed the role of the investor relations function through interviews across 20 firms in the light of rising investor concern about corporate social responsibility (CSR). Whilst they acknowledge that the company's "financial value drivers remain the focus of mainstream investors and analysts" (p. 91) corporate responsibility issues have also begun to enter meetings with mainstream investors. Fundamentally however, relevant disclosure remains far from being integrated with financial orientation such that they report, "what the interviews indicate is that companies are beginning to realise the need for improved disclosure and reporting on social and environmental performance – ahead of mainstream shareholder demands" (p. 95).

Given the increased global attention to sustainability and related reporting, this section will consider whether a sea-change is evident from the literature at that time, evidencing a shift in stock market actor's interest in ESG/sustainability issues.

Briefly, from practice, PricewaterhouseCoopers (2009) reported a growing recognition by fund managers of environmental risks in mainstream investment decision-making. CSR Europe et al. (2003) reported on a survey of 388 fund managers and financial analysts of which 79% of fund managers and analysts indicated that social management has a positive impact on firm value in the long term, and around 50% of them take into account corporate information on social and environmental performance. Moreover, 51% of fund managers and 37% of financial analysts, respectively, would grant a stock price premium to socially responsible companies; findings in stark contrast to that reported by Chan and Milne in the 1990's. However, GRI (2009) highlighted that many companies struggle with how to most effectively communicate their ESG performance to investors so that it can be

"understood and integrated into their decisions… in a way that investors can most readily integrate into their investment analysis" (p. 4). Moreover, ESG reports fail to make the link between a company's ESG strategy and activities and its overall business strategy and activities, and such reporting lacks balance and will "often over-emphasize positive news and not reflect on negative developments" (p. 13), consistent with that found by Deegan and Rankin (1997).

On reporting quality, an issue consistently raised within the literature, Dawkins and Lewis (2003) who surveyed 93 analysts and 50 investors found that 45% and 54% respectively considered companies' information on environmental, social and sustainability performance to be of poor quality. Miles et al. (2002), in an interview-based study (although more focused on the SRI investor community) found an increasing demand for and use of social, ethical and environmental (SEE) information, but that actual disclosure was only partially useful for SRI assessment, as it did not focus on the relationship of the SEE information to shareholder value and financial performance. They report the need for greater investor demand and pressure for disclosure quality such that one interviewee response noted, "once mainstream fund managers start demanding this information companies will have no alternative but to respond to their needs, or face regulatory intervention" (Miles et al., 2002, p. 50). Perhaps reflective of these findings on disclosure quality and lack of integration, Beattie and Pratt (2002) in their survey found that sustainability was ranked in the 4th division out of 5 (and 12th out of 13th in that division) by 'expert' users. Expert users included investment analysts (members of the UK Society of Investment Professionals (UKSIP)), fund managers (employed by leading firms) and corporate lenders (employed by banks engaged in corporate lending). Furthermore, Aras and Crowther (2009) commented that sustainability reporting does not highlight the environmental risks and opportunities of business and, consequently investors may provide capital at an unrealistically low cost, cloaked by a 'veil of ignorance' about environmental risk. Finally, Brown et al. (2009, p. 575) reported that "mainstream institutional investors have so far shown little interest in the non-financial performance data" relevant to ESG/sustainability issues. Indeed, companies interviewed in their study complained that shareholders, investors and employees, their primary target audiences, show little interest in the reports. Reasons for this were commonly attributable to uneven and selective reporting quality by companies, and the selective choosing of reporting frameworks. Indeed, this tension concerning the decision-usefulness of sustainability disclosure to investors versus reporting quality remained a prevalent issue in the literature.

Solomon and Solomon (2006) examined the extent to which social, ethical and environmental (SEE) disclosure was integrated into institutional investment based on interviews with 21 buy-side institutional investors, 14 of whom were mainstream investors. However, whilst such disclosures would, in principle, be decision-useful to investors, they reported that current SEE disclosure was not adequate for investment decisions due to poor reporting quality and lack of integration of SEE information leading to concerns of a silo mentality. To redress they reported an increasing use of private information channels for SEE information. Overall, "almost all of our interviewees asserted that the current level of public SEE disclosure was inadequate for their portfolio investment decisions...However, their attitudes provided evidence that SEE information was decision-useful, and would continue to grow in importance and usefulness in the near future" (p. 573).

Deegan (2004, p. 94) highlighted the increasing importance of environmental factors to fund managers to whom sell-side analysts provided recommendations stating, "fund managers are also using their power to demand that corporations provide environmental performance information. According to Deni Greene Consulting services (2002): fund managers are beginning to use their financial clout to impose environmental disclosure requirements on companies". However, Hunt and Grinnell (2004) in a survey of financial analysts in the US reported that they lacked knowledge about environmental reporting and have a low perceived interest in environmental issues. Following this, Nilsson et al (2008) examined the inclusion of environmental information covering 248 financial analysts' research reports for 33 companies in the chemical industry and the oil and gas industry in North America and in Europe. Content analyses show 65% of the research reports do not contain any environmental information.

At an international level, de Villiers and van Staden (2010) asserted that shareholders would be concerned about the possibility of environmental risk and liability, although due to their economic and reputational consequence, and thus would be more interested in corporate environmental disclosures than before. In a questionnaire-based survey they examined the attitudes and requirements of individual shareholders across UK (105 responses), US (64 responses) and Australia (305 responses) toward corporate environmental disclosure. They found that shareholders are positive about disclosure specifically providing an overview of environmental risks and impacts, the environmental policy, performance against measurable environmental targets and information on a range of environmental costs and for such information to be mandated and to be audited. Across these disclosure areas, levels of support range from 66% to 86% (US); 62% to 84% (UK) and 76% to 93% (Australia) with the most

supported being environmental risks and policy. However, the actual use of information ranged from 44% to 55% for risks and from 45% to 55% on policy. However, in contrast to some of the institutional-based research, individual shareholders (64% UK); (72% US) and (76% Australia) considered environmental information as material for financial decision-making.

In their experimental study, Holm and Rikhardsson (2008) (akin to the earlier Milne and Chan studies) examined the effect of environmental information on short and long-term investment allocation decisions. These were based on financial information and on supplementary environmental information, and its provision (company Gamma) or not (company Beta). Their sample was bifurcated with 98 investors comprised 35 'experienced investors', all with personal experience in investment allocation decisions and 63 graduate business students, termed 'novices'. Both groups consistently allocated a larger relative amount to the company that included environmental information (Gamma) than to the company without environmental information (Beta) consistent with their predicted decision usefulness of the positive environmental information, being (perhaps surprisingly) more pronounced over the short-term. Nonetheless, whilst the results suggest that environmental information disclosure influences investment allocation decisions, environmental information was not rated as being very important when compared to other company financial information.

More starkly, Campbell and Slack (2008) in an interview-based study with 19 UK-based sell-side bank analysts towards environmental reporting and the materiality of environmental risks reported their "general belief that narrative reporting was not immediately applicable nor helpful in the primary tasks of the sell-side which is to construct forecast models and produce written reports for the buy-side" (p. 5) predominantly reflecting financial performance. Indeed, social and environmental reporting was universally considered irrelevant and incapable of influencing a financial forecast and hence "unlikely to be a source of change in respect of social and environmental issues" (p. 12) unless there was a shift in emphasis and demand in capital markets especially from the demand side of reporting information, an issue that is now further considered in more contemporary research.

3.3 A shift in equity market attitudes 2010 to 2020?

In August 2010, The Prince's Accounting for Sustainability Project (A4S) and GRI announced the formation of the International Integrated Reporting Committee (IIRC). The press release stated, "The IIRC's remit is to create a globally accepted framework for

accounting for sustainability. A framework which brings together financial, environmental, social and governance information…in an "integrated" format" (Prince's Trust for Sustainability Project and Global Reporting Initiative, 2010). Indeed, IFAC (2012, p. 7) commented that, "business reporting is typically overly focused on financial performance or, where organizations disclose sustainability or ESG-related information, it is often presented in a disconnected way, so that its relationship to strategy, operations, and financial performance is unclear. This is a key reason behind the proposed integrated reporting framework from the International Integrated Reporting Council (IIRC)". Whilst the Integrated Reporting Framework (IIRC 2013) has been critically debated over its positioning (see for instance de Villiers et al., 2014; van Bommel, 2014; Adams, 2015 and Flower, 2015), nonetheless the IIRC, as well as the mandatory requirements for integrated reporting in South Africa, served to highlight the growing importance of sustainability in the corporate reporting agenda. These developments and the contribution of integrated reporting to sustainability are discussed in chapter 12 (see de Villiers and Dimes)[2], and the emergent sustainability reporting frameworks are discussed in chapter 4 (see Cooper and Michelon).

Further, and building on the Millennium Development Goals, the 2030 Agenda for Sustainable Development, was adopted by all United Nations Member States in 2015, with the 17 Sustainable Development Goals at its core with "strategies that improve health and education, reduce inequality, and spur economic growth – all while tackling climate change and working to preserve our oceans and forests"[3]. ACCA (2016, p. 8) note that "one manifestation of change in corporate reporting is the growth of sustainability reporting". Against this backdrop of increased global awareness of sustainability, the chapter now considers whether equity market views on sustainability/ESG reporting have shifted from the prior decade. Indeed, Milne and Gray (2013) note that more rigorous corporate sustainability disclosure has become an expectation of corporations with rising pressure from investors for improved reporting of ESG and related risks.

However, the challenge regarding a shift in investor opinion is highlighted by Eccles and Serafeim (2013, p. 9) who flag the importance of investor demand for, and support of, sustainability reporting. They argue, "a common complaint made by companies is that most

[2] Specifically for equity market views on Integrated Reporting, readers are also referred to Stubbs et al. (2014); Eccles et al. (2015); Slack and Campbell (2016); Stubbs et al. (2016); Hsiao and Kelly (2018); Slack and Tsalavoutas (2018); Stubbs and Higgins (2018); Abhayawansa et al (2019); Adhariani and de Villiers (2019). And in a South African context, see Atkins and Maroun (2015); McNally et al. (2017).
[3] See https://sdgs.un.org/goals

investors have little interest in sustainability issues, and that their primary focus is short-term performance, such as quarterly earnings". Further, IFAC (2012, p. 3) report "a lack of attention to ESG factors, and the passivity and short termism of some investors, can contribute to short-term thinking by companies" coupled with inconsistencies and insufficiencies in ESG disclosures by companies results in investors marginalising ESG issues. For instance, Fieseler (2011) who interviewed 42 mainstream analysts in Germany on their perceptions of CSR reported that whilst "CSR issues are increasingly becoming part of mainstream investment analysis…for them to play a larger part in the future, investor relations personnel must frame responsibility strategies in a way that is more consistent with the financial community's perspective. In particular, the impact of CSR measures on strategic development" (p. 131). But that at present, "equity analysts largely held a functional view, stressing economic rationales and shareholder value" (p. 142).

Reflective of these challenges, whilst reports from practice all indicate an increased awareness of sustainability issues by investors and analysts, they nonetheless equally report that this is impaired by the quality of reporting, particularly in terms of integration with strategy and risk, comparability over time and between companies and a lack of quantitative measures and specified key performance metrics. For instance, Eurosif and ACCA (2013) in a survey with European investors and analysts (across 18 countries with 94 responses), on their use of ESG information reported, "investors' interest in corporate non-financial information is growing". However, the report highlights the disconnect of reporting to business strategy and risk, a lack of comparability and insufficient information for them to assess its financial materiality with quantitative KPIs with 78% viewing non-financial reporting as not being adequate for their needs (consistent with IFAC, 2012). Radley Yeldar (2011) in a report commissioned by GRI and A4S with 34 investors and 35 analysts found that 79% were influenced by sustainability reporting information in investment decision-making. It should be noted that the findings are drawn mostly from socially responsible investors with 68% of the respondents being directly engaged in socially responsible investment, with the remainder acknowledged as having at "least an interest in such issues" (Radley Yeldar 2011, p 12). However, the report referred to issues of comparability such that investors and analysts find it hard to benchmark extra-financial and particularly social performance information. More recently, CFA Institute (2017) reporting on global perceptions of ESG investing (sample size 1,588 respondents), highlighted the importance of risk analysis and client-led demand were the main reasons to take ESG integration into consideration and that 73% of respondents take ESG issues into account. However, they are

again critical of a lack of comparability (50%), a lack of quantitative ESG information (55%) and issues concerning data quality issues and assurance.

From a direct investment house perspective, Choi (2016) (CEO of Morgan Stanley Institute for Sustainable Investing) reported on a 2014 survey of 1,000 active individual investors finding that "over 70% of the investors expressed interest in sustainable investing—and 65% of the respondents said they believed that sustainable investing would become even stronger during the next five years" (p. 62). Further, in a joint survey by Morgan Stanley with Bloomberg Sustainable Finance undertaken in 2015 with over 200 global pension funds, endowments, and insurance companies, Choi (2016) reports that that asset owners have a strong positive attitude toward, and an increasing level of engagement with, sustainable investing strategies.

However, whilst acknowledging investor criticisms, not all reports affirm the importance, or more specifically the decision-usefulness, of sustainability/ESG reporting information. For instance, Hsiao and Kelly (2018, p. 6) report on EY's (2015) global survey of more than 200 institutional investors. This finds that "24% per cent considered ESG information played a pivotal role in their investment decisions, but significantly that 50% were only occasionally or seldom influenced by such information, and 26% considered it immaterial because of the difficulty in determining its relationship with financial performance and issues with assurance and comparability". McKinsey (2019) in a global survey 107 of executives and investors (covering 50 companies, 27 asset managers, and 30 asset owners) and interviews with 26 asset managers, asset owners, corporations, standard-setting organizations, nonprofit organizations, and academic institutions reported that investors cannot readily use companies' sustainability disclosures to inform investment decisions. Significantly the findings highlight that "investors want companies to provide more sustainability disclosures that are material to financial performance" (p. 5) and raise issues of comparability and inconsistent reporting due to a lack of a mandatory reporting framework. Finally, Pinney et al (2019, p. 89) whilst recognising a marked increase in interest in ESG by the largest asset owners emphasise the continued lack of a "generally accepted definition of ESG and standardised way for companies to report on material ESG performance. This is further complicated by the lack of consensus between the major ESG rating and ranking agencies, which often provide widely different rankings for the same companies and are using different and often non-transparent methodologies to account for significant data gaps" (and see Conway, 2019).

The academic literature similarly voices concerns regarding the quality of

sustainability/ESG reporting, raising, in particular, issues of impression management and corporate legitimacy seeking with a focus on good news (harking back to the early studies of Milne and Chan and Deegan and Rankin) and a consequent lack of balance in reporting as well as issues of comparability and consistency. For instance, in their theoretical study drawing on legitimacy and accountability constructs in sustainability reporting, Comyns et al. (2013, pp. 231-2) report, "the overall consensus of this research is that although the number of sustainability reports has increased, reporting quality remains poor…[such that] sustainability reporting appears as symbolic action". Further, Cho et al. (2015b, pp 15-16) in a market-based comparison review capturing the change in such reporting over time using 1977 and 2010 Fortune 500 data examines whether CSR disclosure is valued by market participants. They report, "CSR disclosure…is not positively valued by investors…as such disclosure may still largely be driven by concerns with corporate legitimacy, and still fails to provide information that is relevant for assessing firm value". Indeed, in their review, Hinze and Sump (2019, p. 146) reflect, "in summary, recent surveys and interview studies on analysts' perceptions of CSR fail to uniformly support an increasing interest in CSR or a shift in analysts' perceptions towards a positive assessment of CSR".

In relation to user-based research, in sequential studies, Ardvisson (2010; 2014) firstly found that management teams argue that the increase in interest for CSR information comes from the actors in the stock market and subsequently tested this proposition by interviewing 17 sell-side financial analysts. This latter study reports that analyst interest in CSR information has not changed in a way that would justify an increased focus on CSR in corporate communication. "Thus, it appears as if management teams have deluded themselves and become victim to what Christensen and Cheney (2000) refer to as "self-seduced and self-absorbed", i.e. seeing things that are not really there" (p. 217). Further, Arvidsson (2014, p. 210) reports that actors in the stock market express "mistrust towards this information and continue to have a meagre interest in it" and that such reporting is perceived as "little more than window dressing or a public relations exercise" (p. 213). Helfaya et al (2019) examine the quality of corporate environmental reporting through a questionnaire-based survey of 177 users including 48 financial analysts (and 86 preparers). Although the findings are not analysed across sub-categories of users and are presented globally for preparer and user groups respectively, they highlight the importance of information quality especially with regard to completeness, accuracy and reliability of disclosure especially in relation to targets and quantitative non-financial information.

In their interview and questionnaire study with 61 Polish sell-side analysts and buy-

side analysts employed in financial institutions based in Poland, Krasodomska and Cho (2017) directly examine their use of non-financial information related to CSR issues. The results reveal that financial analysts rarely use CSR disclosures (74% of the respondents use them never, very rarely or rarely) and that analysts' attribute very little importance to such information consistent with the earlier reporting studies on analysts' report content (Hunt and Grinnell, 2004; Nilsson et al., 2008). However, although such users would be receptive to more frequent use of CSR-related information, they are critical of current disclosure highlighting a low assessment of reporting quality due to lack of reliability, comparability across companies and managerial bias.

Finally, given the increased use of reporting frameworks over time, Diouf and Boiral (2017) in a Canadian study examined the quality of sustainability reports using the GRI framework. They carried out 33 interviews with a range of stakeholders including fund managers and analysts. Significantly, the GRI principles cover six main aspects of sustainability reporting – balance, comparability, accuracy, timeliness, clarity, and reliability of the reports to users. Whilst the findings confirmed the increasing use of the GRI by preparers and the "importance of standardization for the measurement of corporate sustainability performance…[concerns were raised] that many of these reports are not balanced, that they are trying to present the good side of the coin" (pp. 652-3) such that impression management strategies continued to be used by companies emphasising the positive aspects of their sustainability performance and obfuscating negative outcomes (and see archival/empirical studies such as Cho et al., 2012; Boiral, 2013; Cho et al., 2015a; Cho et al., 2015b; Boiral, 2016; Talbot and Boiral, 2018). Further, and specifically relevant to investor usefulness, they highlight "the difficulty of analyzing performance over time and in determining quantitative targets for the coming years, the differences in the units used to quantify some indicators, [and the] overall lack of timeliness, precision, clarity, and reliability in the information reported by companies" (p. 657). Similar findings are reported by Chiba et al. (2018) in their analysis of sustainability reporting by Quebec local government ministries. They argue that "sustainability disclosure is shaped by the search for corporate legitimacy rather than a desire to release reliable information. As a result, sustainability reporting tends to obfuscate negative events...and to foreground positive outcomes that are likely to improve corporate image" (p. 329).

3.4 Reflections on equity investor perspectives.

This chapter has considered the substantial research conducted directly with equity investors

comprising fund managers, buy-side and sell-side analysts and specifically their use and the usefulness of sustainability reporting information to them over time. This section reflects on the prime research methods employed, whether these methods have changed over time and importantly highlights the key emergent themes arising from the research enabling comment on whether there has been a shift in investor sentiment towards such reporting and its usefulness to them.

Commencing with the early studies in this field, in the pre-2000 period, postal survey and questionnaires were the dominant research approach often employing an experimental method. This would involve social and environmental related reporting extracts (not the wider sustainability reporting lens used in later studies) drawn from the annual report, or experimental studies using varying levels of good or poor performance and its reporting. This general body of early research revealed an ignorance of non-financial reporting and little appetite of demand for ESG or sustainability information by equity investors. Overall, it was generally perceived as lacking decision-usefulness to them with a clear focus on financial performance. Hence, only in instances of direct financial consequence was sustainability regarded as an issue, although this was often obfuscated in its reporting raising more general concerns as to a 'good news' bias in such reporting.

Following these early studies, in the period 2000 to 2010, academic research, whilst still using surveys/questionnaires, the use of interviews directly canvassing investor opinion became more common, methods that remained commonplace in the final period to 2020. In the period to 2010, the research showed an increased general level of investor awareness in sustainability issues, widely noted in practice-based publications, reflecting its greater prominence evident in reporting frameworks, such as GRI, global attention through the Millennium Development Goals and the emergence of investor sustainability-related fora such as PRI and SIF. In general, however, despite the increased awareness in sustainability, and private shareholder interest and specifically those more involved with social and ethical funds, criticisms regarding the credibility and lack of balance of such reporting remained, a finding largely unchanged from the prior period. This mitigated its decision-usefulness to mainstream investors in contrast to their continued focus on financial performance and related metrics. Increased quality of reporting through more explicit investor-led demand was often referred to serving to enhance its decision-usefulness to them and to perpetuate future reporting balance and credibility.

The final period, 2010 to 2020, revealed continued investor appreciation of sustainability related issues, evidence of their demand for greater disclosure quality and the

growing importance of sustainability in the corporate reporting agenda through the emergence of further reporting frameworks, such as integrated reporting. However, despite this, whilst the literature confirms an increasing level of investor awareness and appreciation of sustainability and related reporting, its decision-usefulness to equity market participants, in general, remained patchy and somewhat limited. This primarily reflects their enduring criticisms towards its reporting quality and principally issues of comparability, quantifiable metrics and performance with concerns over a lack of balance. Indeed, more prevalent in the final period are those academic studies that highlight the use of impression management within such reporting with respect to corporate reputation and image. As such, despite far greater awareness, the early investor criticisms of reporting quality impairing its decision-usefulness to them largely remain and their demands for more clear reporting balance and its impact directly relevant to financial performance. Indeed, on this latter issue, as Slack and Campbell (2016, p. 14) reflect, "bluntly, are equity investors, as a key intended user, driven by short-term (financial) pressures augmented by quarterly reporting, and therefore privileging that information over information on longer-term sustainability issues and value creation?", a question that the chapter will return to in Section 5 considering current market views on sustainability especially in the light of Covid-19.

4. Providers of debt finance and sustainability reporting research

Whilst the majority of the literature canvassing views of capital market participants in relation sustainability reporting, its use and decision-usefulness to them, is positioned in the equity market, nonetheless, there are a small number of studies that have engaged with providers of debt finance that are now considered.

Environmental considerations in debt financing decisions were highlighted by Warford and Parlow (1989) and that such factors would be more evident in the future due to an increasing awareness of environmental issues and related risks in lending. Tilt (2007, p. 108) reports that "in 1988, the World Bank reported that over 38 per cent of all of its loans were described as having important environmental objectives, which covered at least 5 per cent of the project cost. Indeed, Rankin (1996, p. 126) highlights, "organizations which show that they are environmentally aware ...may also find that they are able to attract finance at a lower cost than would otherwise be possible" (and see Goss and Roberts, 2011). Such an assertation is consistent with that argued by Hickman (2020) that companies engaging in CSR activities receive favorable treatment from debtholders and publicly-traded debt could motivate increased CSR reporting as dispersed bondholders are subject to greater information

asymmetry. “Hence, publicly-traded debt could motivate some privately-held companies to publish CSR reports to communicate to their dispersed creditors” (p. 211).

Specifically on bank lending, Thompson and Cowton (2004) examined the extent to which UK banks incorporated environmental considerations into their lending decisions. They found that 87% of banks included an appraisal of environmental risk as part of their credit risk assessment procedures and as a consequence, a poor environmental record, rather than the industry sector, was a reason for the withholding of finance. Bhimani and Soonawalla (2010) examined the application of the Equator Principles in lending decisions to embed sustainability. The Equator Principles require lenders to assess and monitor the impact of finance loans in relation to relevant environmental and social risks associated with the underlying project and hence the lending decision should be refused if these conditions are not complied with. Specifically, they analysed HSBC which adopted the Equator Principles in 2003 (the year of inception) and applies these to all project loans above $10m with specific sector policies for sensitive sectors including forestry, metals, mining, water, energy and chemicals.

Developing this reasoning of increased environment sensitivity in lending decisions, Campbell and Slack (2011), highlighted the reputation risk to lenders stemming from decisions with significant environment implications. They reported on Royal Bank of Scotland and the pressure group Rising Tide (2007) due to levels of lending in the oil and gas industry and ABN Amro and Société Générale and the pressure group Rainforest Action Network (RAN) through their $2 billion financing of Russia’s Sakhalin II oil and gas project. Tangentially, and consistent with reputational risk, Kolk et al, (2008) found that Citigroup, JPMorgan and Morgan Stanley all issued restrictive guidelines for new coal investments due to the increasing regulatory and environmental risks and potential reputational impact. Despite this, Campbell and Slack (2011) based on interviews with 19 London-based sell-side bank analysts examined the decision-usefulness to them of bank annual report environmental narratives and the importance of environmental risks in the assessment of bank risk profile and valuation as well as any reputation risk concerns. Their findings revealed that the recognition of the materiality of environmental risks in banks is uncommon among sell-side analysts and that environmental narratives are often ignored and regarded as perfunctory. For instance, one of the respondents commented, “frankly I’d ignore it really” and went on to comment that, “pretty high up the list [of the most immaterial parts of the annual report] would be the environmental report” (p. 59). Further another respondent was critical as to the actual quality of the disclosure, “it sounds bad, but from our point of view at the moment this

CSR/environmental [disclosure] is close to useless" (p. 59) harshly reflecting some of the criticisms and resultant lack of decision-usefulness reported on in Section 3 in relation to equity market views.

5. Where we are today? Covid-19 and global sustainability standards.

It is apposite to now reflect on capital market perspectives brought about by the Covid-19 crisis, a global pandemic with significant economic and hence market-based consequences, and the (somewhat ironic) need to consider the wider framing in which companies operate, a feature inherent in sustainability reporting. Indeed, as Adams and Abhayawansa (2021, p. 1) argue, "the pandemic put the 'S' in ESG (environmental, social and governance) under the microscope and provided a reason to re-assess the 'E'. The fragility of supply chains, labour markets, credit quality and liquidity are weaknesses in the financial system revealed by the pandemic (CFA Institute, 2020). And there's increasing concern that climate change could further expose the vulnerability of the financial system and test its resilience (Franklin, 2020)". What is clear from practice-based reports (and echoed in very recent academic studies, such as Adams and Abhayawansa (2021), is the increasing importance of sustainability factors underpinning investment decisions and the related flow of funds into both equity and debt markets. For instance, UBS (2020, p. 1) in a report, 'Sustainable investing after COVID-19' notes, "the [Covid-19] crisis underscores the relevance of ESG considerations to company performance and investment returns, and we expect that this will continue to influence corporate and investor actions going forward" and continues, "COVID-19 has elevated the importance of how companies operate and accelerated the already increasing relevance of ESG considerations to investors, in our view" (p. 2). Furthermore, the report highlights the continued growth of the green bond market (now with a market size around EUR 750bn), which has increasingly become used by governments to fund environmental projects. Moreover, in April 2020, the issuance of bonds with ESG characteristics, such as green and sustainability bonds, increased by 272% year on year.

Indeed prior to the pandemic the World Resources Institute (2019, p. 1) reported that investors, "increasingly view global sustainability challenges as material to long-term financial performance, as the visible impacts of climate change… more investors are pursuing strategies that consider relevant environmental, social and governance (ESG) factors". However, despite this, drawing in interviews with 30 investors from 25 investment firms, the World Resources Institute report echoes prior criticisms of ESG reporting data that prevents a true scaling and mainstreaming use ESG data to evaluate the sustainability context

of investments due to inconsistent reporting metrics and that "most disclosures come through as check-box yes-or-no responses, generic boilerplate language or tailored narrative, rather than robust quantitative performance indicators" (p. 3). Further, the Sustainability Accounting Standards Board (SASB) (2021) report the low level of investor confidence in ESG disclosure usefulness and site Goldman Sachs (2017) that reported that only 12% of such metrics were direct performance data and 22% related to targets with inherent concerns of comparability, measurement bases and methodologies and unclear consistency.

The tension between sustainability reporting and its decision-usefulness to investors is also noted by IIRC and Kirchhoff (2020) in an interview-based investor research report with 10 buy and sell-side equity market participants in Germany (and one based in Switzerland). They report that investors increasingly appreciate the linkage between company performance on a range of environmental, social and governance factors and their ability to deliver profits over the longer term. For instance, one equity analyst confirms that "it is quite clear that the non-financial focus has massively improved and that the focus is now very prominently on what happens outside the financial figures – which is desirable… These are important factors that deserve to be presented more prominently in a report, and they really do add value for shareholders" (p.17). However, the report also recognises that current ESG reporting can seem like simply "ticking the box" rather than a "serious, deep integrated measurement" (p. 13).

At a more global level and reflective of the current (and highly contentious) debate surrounding reporting frameworks (see for instance Adams and Abhayawansa, 2021) despite, as noted, the now widespread use of GRI, the IIRC and Kirchhoff (2020) highlight issues of multiple reporting guidelines adding to a lack of consistency and comparability and the drive towards a global standard. Indeed, in September 2020, five framework- and standard-setting institutions, Carbon Disclosure Project (CDP), Climate Disclosure Standards Board (CDSB), GRI, IIRC and SASB co-published a shared vision of the elements necessary for more comprehensive corporate reporting and a joint statement of intent to drive towards this goal. Further, the report highlighted the intention of the IIRC and SASB to merge in into a unified organisation, the Value Reporting Foundation, which was formalised in June 2021[4], and notes that "The Value Reporting Foundation will maintain the Integrated Reporting Framework, advocate integrated thinking, and set sustainability disclosure standards for

[4] See, https://www.valuereportingfoundation.org/news/iirc-and-sasb-form-the-value-reportingfoundation-providing-comprehensive-suite-oftools-to-assess-manage-and-communicate-value/

enterprise value creation" (p. 3). GRI[5] Chairman, Eric Hespenheide (GRI, 2020) stated, "understanding the financial risks related to these sustainability impacts on a company's bottom line and value creation are critical for providers of financial capital. The formation of the Value Reporting Foundation represents a significant step towards a better representation of sustainability related risks in financial reporting".

In a similar timeframe, The IFRS Foundation sought to establish a Sustainability Standards Board and develop a single set of sustainability standards that would provide financially material sustainability information (and see Barker and Eccles, 2018; 2019). To that end, the Trustees of the IFRS Foundation published a Consultation Paper on Sustainability Reporting in September 2020 feedback on which, they reported, confirmed an "urgent need for global sustainability reporting standards and support for the Foundation to play a role in their development" (IFRS 2021). In April 2021, the Trustees issued a Feedback Statement that summarised the significant matters raised by respondents to the Consultation Paper on Sustainability Reporting although not percolating to any changes in strategy. An Exposure Draft was also issued that outlined the proposed amendments to the IFRS Foundation Constitution to accommodate an International Sustainability Standards Board (ISSB) to set IFRS sustainability standards.

The outcome of these developments is unknown but highlights the critical significance and importance of sustainability reporting and its intended decision-usefulness to stakeholders including the capital markets. Clearly such developments are rich for further research through examining the respective developments of the bodies involved and specifically the comment letters and other public debate forums of commentary, especially considering the views of investors. On the latter, this may provide insight into a real or more symbolic use of sustainability reporting, or whether this remains overshadowed by financial performance metrics with a focus by them on more short term rather than longer term issues.

Beyond this, it is evident from this chapter that whilst there exists a substantial body of research that has engaged with the equity market, far more research could usefully be performed with a focus on the debt and bond markets in relation to how ESG/sustainability reporting is factored into decision-making and their implications for financing. This is especially relevant in consideration of the growth in green and sustainability bonds.

However, it remains evident, that despite a significant growth in sustainability/ SRI

[5] GRI is a founder member of IIRC, and see https://www.globalreporting.org/about-gri/news-center/2020-11-25-gri-welcomes-consolidation-of-value-reporting-organizations/

based investment, and especially in the light of Covid-19, IIRC and Kirchhoff (2020) still highlight the need for greater investor pressure on companies for sustainability reporting quality such that, "If investors would like to see more reporting of this nature, how could it be encouraged? *Investor pressure is essential*" (p. 5) (emphasis added). This acknowledges the need for enhanced reporting quality to stimulate greater investor demand consistent with that noted by Slack and Tsalavoutas (2018) and in the earlier studies such as those by Miles et al. (2002), Hockerts and Moir (2004); Campbell and Slack (2008) and Eccles and Serafeim (2013). As such, reporting may serve to address Gray's (2006, p. 71) critical concern that, "indeed, I fear we must conclude that sustainability is an issue of the profoundest importance to all peoples - including even economists, investors and aggressive CEOs - and that its implications require a non-linear shift away from current measures of social responsibility and performance...Until corporate reporting reflects this we are misleading ourselves and failing to address the matters of direct concern" relating to the ecological footprint, including rising and acknowledged climate change issues, and the destructive impact on the global ecosystem.

If wider investor-led pressure is more forthcoming it may help drive the greater embeddedness and contextualisation of sustainability reporting information and its quality such that it becomes more decision-useful to them. Furthermore, this may also trigger a wider realisation that sustainability issues should not (or can not) be simplified into simple metrics regarded as almost a by-product of the financial reporting system. Increasingly, investors are aware of the significance of sustainability (and its direct impacts on corporate risk and performance) signaling a culture shift from largely a historical ignorance of issues to now one of more active engagement. To further shift demand, investor fora could more explicitly report on good practice and showcase examples of sustainability reporting clearly highlighting its decision-usefulness to capital market users with appropriate endorsements. This may serve to drive up reporting quality and provide preparers and with greater incentive to satisfy user-led investor demands with more balanced reporting. For instance, reflecting sustainability through corporate strategy, the reporting of clear and consistent sustainability related targets, with consistent performance reporting and linked KPI's of equal prominence to financial performance metrics. The flagging of key identified risk factors in relation to sustainability, their link to strategy objectives, how they are managed and what actions have been taken to mitigate identified risks.

Ultimately, this may trigger a fundamental shift of emphasis in the use of sustainability reporting by capital market users and its consequential decision-usefulness to

them away from short-term financial metrics to more long-term issues inherent in sustainability reporting, significant for future cashflows and enterprise value. Fundamentally, sustainability reporting serves to encapsulate the global environment within which businesses operate, with appropriate links to governance, strategy, business model and risk, indeed on which financial performance measures are ultimately dependent.

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