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Compliance of Sustainability Reporting and Firm Financial Performance: An empirical analysis of selected BSE Listed Firms

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Abstract: *Compared to Financial disclosure non-financial disclosure and its importance on the firm's performance and valuation is less researched area and it is less tested concept by investor while taking any investment decision. So objective of this paper is to check compliance of non-financial disclosure as per the framework issued by GRI from time to time with its standard G4 recently, it is checked in two steps. In first step Company-wise overall sustainability reporting (Non-Financial Disclosure-ESG Disclosure or Triple Bottom line)impact on firms Operating performance (ROA) and Financial Performance(ROE). And in the second step importance of individual dimensions of sustainability (i.e., item wise) of Economic, Environmental & Social aspects related disclosure index on firms operating and financial performance is done. Study has run univariate and multiple regression analysis models to find the relationship between different disclosure index and its Performance. Moreover a ANOVAs test was run to check the significance of the model. Results of tests found that there is 45% and 71% variability in the dependent variable ROE & ROA of the business with overall sustainability related aspects (EES), there is a more impact on operating performance of the business as compared to financial by sustainability related disclosure and only environmental related aspects positively affecting financial performance of the business.*

Key words: *Sustainability Reporting, GRI, ROE (Return on Equity) & ROA (Return on Assets)*

1. INTRODUCTION:

Non financial reporting such as sustainability and CSR Reporting is fairly a recent trend in corporate reporting. It has expanded over the last twenty years. Corporate sustainability reporting has a history going back to environmental reporting. The first environmental report was published in 1980s by the companies in chemical industry which had a serious image problem. The other group of early adopters was a group of small and medium sized businesses with very advanced environmental management systems. It is an organizational report that gives information about economic, environmental, social and governance performance. There are a variety of reasons that companies choose to produce these reports, but at their core they are intended to be vessels of "transparency and accountability" Often they also intend to improve internal processes, engage stakeholders and persuade investors.

The Sustainability reporting also referred to as Business Responsibility reports or Triple Bottom line reporting. Elkington (1998) developed the term "triple bottom line" to emphasize on three aspects - profits (economic), people (social), and planet (environmental). Sustainability Reports are published by firms to provide a description of their triple bottom line performance and to show the commitment of firm towards its diverse stakeholders. According to G3.1 Sustainability Reporting guidelines developed by Global Reporting Initiative (2011) - The environmental dimension of sustainability concerns an organization's impacts on living and non-living natural systems, including ecosystems, land, air, and water". The social dimension of sustainability concerns the impacts an organization has on the social systems within which it operates. The „economic dimension" of sustainability concerns the organizations impacts on the economic conditions of its stakeholders and on economic systems at local, national, and global levels." (Agarwal, Sep-2013)

Sustainability disclosure deals with the Environmental, Economic and Social aspects of the business. Many studies show that sustainability reporting even includes aspects related to corporate governance but which is not. Business entities have to separately prepare the corporate governance report as per the provisions given under clause 49 of the SEBI regulation act. Sustainability reporting is to be prepared as per the GRI guidelines. In India there is a national voluntary guidelines issued by the Ministry of Corporate Affairs on Business Responsibility Reporting in July 2011.These guidelines furnishes principles and layout of corporate responsibility reporting for all Indian companies including MNCs and SMEs.it is mandatory for the top 100 listed companies to prepare BRR as per the NVG w.e.f 13/08/2012.Some companies are hosting their SER on separate website too and provide its link with the existing Annual Report. Many companies in India have started following GRI guidelines in preparation and presentation of SER.

Considering the sustainable development as an emerging and contemporary topic among the corporate of India this study has tried to gain knowledge on it .By following the GRI guidelines study has constructed a sustainability disclosure index and tried to find level of compliance by selected firm and its impact on the financial performance of the firm .The following paragraph of the paper includes Section-II Literature Review Section-III Research methodology Section-IV Data Analysis Section-V Findings and Suggestion and lastly limitation, Scope for further research, Conclusion and References .

2. LITERATURE REVIEW:

Foreign studies:

The impact of Sustainability reporting on firm profitability by lencee. L Whet man has explored on how sustainability affects profitability between high and low institutional ownership. Study has used lagged regression profitability by taking csr as independent variable (Dummy for sustainability reporting and ROA, ROE & NP margin as dependent variable, taking size, capital structure and percentage of insider and institutional ownership as control variable. The findings suggests that by engaging in sustainability reporting, firms with lower institutional ownership shows significant improvements in financial performance in the subsequent year after reporting. (Whetman, 2017) **Corporate Sustainability disclosure practices of Indian companies: An empirical analysis by Dr. Gurdeep Singh Batra** has measure the extent and quality of corporate sustainability disclosure. And relationship between sustainability disclosures and company characteristics like sector classification, size and age by framing corporate disclosure index score as per GRI Guidelines by applying statistical tools mean and S.d for sectorial differences and ANOVAs test to find any significant differences between sectors, size and age in terms of their sustainability disclosure scores and results shows that size and sectors are significantly associated with level of sustainability disclosures made by companies. While age is not. Moreover profile wise low profile sectors demonstrates high GE & SI Scores but low EC Scores. Larger companies in terms of market capitalization and total assets have propensity to make more and better sustainability disclosures as compared to smaller companies. (Puneet Sikand, ;May 2014) **ESG and Corporate Financial Performance: Empirical Evidence from China's Listed Power Generation Companies by Changhong Zhao** In this article, Researchers have studied China's listed power generation groups to explore the relationship between ESG performance and financial indicators in the energy power market based on the panel regression model. The results show that good ESG performance can indeed improve financial performance, which has significant meanings for investors, company management, decision makers, and industry regulators (Changhong Zhao 1, 2018) **The impact of Sustainability Reporting on Company Performance by N.Burhan by** using the GRI guidelines on EES disclosure an index of different sustainability reporting elements were constructed and two models were developed. At first stage impact of overall sustainability reporting on financial performance (ROA) & in the second stage individual independent economic, environmental and social disclosure index scores impact were checked on company performance i.e., ROA with univariate and multiple regression model respectively. An ANOVA test is used to measure overall significance of the model. The finding of the model suggests that there is 7.3% variation in the financial performance of the firm with sustainability reporting. The Environmental & Economic variables are negatively affecting company performance whereas Social disclosure items have a positive impact over financial performance of the business. (Rahmanti, August 2012,) The Effect of Sustainability Reporting on Financial Performance: An Empirical Study Using Listed Companies by Krishna Reddy,1, Lucus W. Gordon this study first aims to investigate whether sustainability reporting by listed companies in Newzealand and Australia has an effect on their financial performance and value. Second, whether sustainability reporting has a similar effect on the listed companies in smaller economies compared to listed companies in larger economies. Cross sectional dummy regression of AR(Event Study Methodology-Market Model For AR Computation) against sustainability report type (CSR, Annual, environmental, sustainability report) and cross sectional dummy regression of AR against sustainability Report type, Country and Dirty industry membership for all. There is a significant relationship found between market return and sustainability reporting between Australian companies but not for Newzealand Companies. And out of four only CSR type of report has influence over market return of Newzealand Companies. (Krishna Reddya, Vol VI, Issue 2, December 2010) Sustainability Reporting under G3 Guidelines: A Study on Constituents of Bovespa Index by Aparna Bhatia, Siya Tuli ; study shows the extent of sustainability disclosure practices by Brazilian firms for the time period of 2006-07 to 2010-11.the study has developed item wise disclosure index and used the content analysis technique as a data collection tool. Moreover extent of disclosure further analysed at three different levels i.e., Company Wise, Item-wise and Industry-wise analysis is performed. An ANOVA test is applied to check differences in disclosure across the industries. And it was found that paper and pulp industries are having the highest disclosure Scores 87.97%. The Outcome concludes that though sustainability reporting is voluntary in Brazil, yet the country is progressively endeavoring in this field. (Tuli, 15,May 2017).

Impact of Sustainability Reporting on Financial Performance of Selected Quoted Companies in Nigeria the study examined impact of sustainability reporting on selected quoted firms in Nigeria between 2012 and 2016. Data for the study generated from the financial reports of the companies and was analyzed with the panel least square technique. Study has constructed disclosure index on expenditure related to the different Economic, environmental and social activities of the business as independent variable and P/E ratio as a dependent variable and study has concluded that expenditure on economic activities and environmental activities are significantly affecting the financial performance of the business but expenditure on social activities are not much affecting the financial performance of the business. (Firms, 2017) **The Impact of Sustainability Practices on Corporate Financial Performance: Literature** Trends and Future Research Potential by Ali Alshehhi 1,* Haitham Nobanee 1 and Nilesh Khare 2 Study presents analysis of literature concerning the impact of corporate sustainability on corporate financial performance. A study of 132 papers from top tier journals were shortlisted and it is found that 78% of publication report a positive relationship between sustainability and financial performance. It is found that there is a very less research done on non-financial disclosure in developing countries. More research is needed to facilitate convergence in the understanding of the relationship between corporate sustainable practices and financial performance. (Ali Alshehhi 1, 2018)

10. Impact of Sustainability Reporting on Firm Performance of Companies in India

"Impact of sustainability reporting on Firm Performance of companies in india.by priyanka Garg. The present study has made an attempt to investigate the company wise compliance of sustainability disclosure guidelines given by GRI for the time period of 2008-2012 of BSE GREENEX Companies. And to study the sustainability reporting practices of companies over the period of the study. According to the results of paired sample t-test it is found that there is a improvement in sustainability disclosure practices of the companies over a period of time. Moreover impact of sustainability practices on performance of the business has been done with regression analysis taking ROA & Tobin's Q as dependent variable and Sustainability scores (ESG) of the study period as independent variables. And it is found that in long run sustainability disclosures have positive impact on the business whereas in short run not. (Garg, 2015).

"Link between Corporate Environmental Disclosure and Firm Performance" – Perception or Reality? By P. Malarvizhi & Ranjani Matta Primary objective of this research is to understand whether there is any significant relationship between Corporate Environmental Disclosure (CED) and firm performance of selected companies listed in Bombay Stock Exchange (BSE), India. This research uses content analysis methodology by developing an environmental disclosure index (EDI) and formulating hypotheses to test the association between firm performance and level of environmental disclosure through a sample of 85 companies from chemical, energy and metal sector listed in BSE. A regression model with EDI as dependent variable and return on capital employed (ROCE), return on assets (ROA), net profit margin (NPM) and earnings per share (EPS) as independent variable is used to analyse data for this research. Results show there is no significant relationship between the level of environmental disclosure and firm performance. (P. Malarvizhi) **"Rising standards of sustainability reporting in India: A study of impact of reforms in disclosure norms on corporate performance" by puneet Goel.** This paper aims to look in to sustainability reporting practices by top companies listed in Bombay stock exchange and its impact on financial performance. 68 companies were selected from the top 100 in the list of ET500 for 2016. Self-constructed sustainability reporting score has been computed for each company for the financial year 2012-2013 and 2015-2016. The two periods represent pre- and post-disclosure reform periods in India. A sustainability reporting scale has been constructed using 16 parameters of sustainable performance based on social, environment and governance aspects as reported in the annual report, sustainability report and business responsibility report. It has been found that there is a significant improvement in sustainability reporting by Indian companies after the introduction of disclosure reforms. Different sectors show significant difference in the sustainability reporting during pre-reform period but as the sustainability reporting improves after the reforms, sector difference reduces. Sustainability reporting is a significant predictor of financial parameters of return on sales, return on equity and Tobin's Q in pre-reform period, but in the post-reform period, no significant impact was found on financial performance. (Goel, 2018)

tabase.

Research Problem: The non-financial disclosure is in a very infant stage in India. By the year 2011, globally there are about 8691 sustainability reports published based on GRI [4]Framework. With the growing significance of sustainability issues at the global level, companies in India are also getting ready to embrace reporting on sustainability to enhance competitiveness. As per the one article published by icsi there are only 47 companies in India disclosing their sustainability performance. Out of 8691 reports only 122 reports are published by Indian companies. This has inclined a researcher to find out the level of sustainability disclosure practices in India as per the GRI Guidelines. Moreover recently many investors have started considering non-financial disclosure aspects in their investment as a green initiative and reducing environmental footprints via their investments. This will affect the operational and financial performance of the business so study has tried to explore the relationship between sustainability reporting and its impact on operational (ROA) and financial (ROE) performance of the business.
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3. RESEARCH METHODOLOGY:

Research Design: It is an empirical and descriptive type of research .The data sources used in the study are annual reports (Financial, Sustainability reports) of the sample companies, research articles used in the journals and magazines etc. Study has used content analysis method for data analysis by considering sustainability reporting standard given by GRI –G4 and analyzed it for the time period of 2015-16 to 2017-18 by developing disclosure of index for ESG data reported in an annual report of the study. Total 70 different aspects were covered under the study by giving weights of ‘0’(For non-disclosure)and 1,2,3,4….(as per the level of disclosure.)

Research Objectives: 1. To Study the Compliance of Sustainability related disclosure of business as per GRI G4 Standards and to analyze the impact of it on the operating and financial performance of the business.

Hypothesis: 01
H0: There is not a significant impact of SDI[1] on the financial performance of the business.
H1: There is a significant impact of SDI[1] on the financial performance of the business.
Hypothesis: 02
H0: There is not a significant impact of SDI[1] on the Operating Performance of the business.
H1: There is a significant impact of SDI[1] on the Operating performance of the business.
Hypothesis: 03
H0: There is not a significant impact of ENVD[1], ECND[1], & SD[1] impact on the financial performance of the business.
H1: There is a significant impact of ENVD[1], ECND[1], & SD[1] impact on the financial performance of the business.
Hypothesis: 04
H0: There is not a significant impact of ENVD[1], ECND[1], & SD[1] impact on the Operating performance of the business.
H1: There is a significant impact of ENVD[1], ECND[1], & SD[1] impact on the Operating performance of the business.

The above hypothesis are being generated to explain the impact of Sustainability disclosure score on the financial & Operating performance of the business and individual EES Score on the financial & Operating performance of the business by testing equation (1,2,3&4) below as the base model. OLS regression method is used to test the significance of the coefficient of the independent variables by considering **Size, Capital Structure and Growth of the business as control variables.**

$\mathbf{ROE_{it}} = \alpha_0 + \alpha_1 SRI^{2,3}_{it} + \alpha_2 Size_{it}^{11} + \alpha_3 CS_{it}^{11} + \alpha_4 Growth_{it}^{11} + \sum_{it}$ ....(1)

$\mathbf{ROA_{it}} = \alpha_0 + \alpha_1 SRI^{2,3}_{it} + \alpha_2 Size_{it}^{11} + \alpha_3 CS_{it}^{11} + \alpha_4 Growth_{it}^{11} + \sum_{it}$ ....(2)

$\mathbf{ROE_{it}} = \alpha_0 + \alpha_1 ENVDI_{it} + \alpha_2 ECNDI_{it} + \alpha_3 SDI_{it} + \alpha_4 Size^{11}_{it} + \alpha_5 CS_{it}^{11} + \alpha_6 Growth_{it}^{11} + \sum_{it}$ ....(3)

$\mathbf{ROA_{it}} = \alpha_0 + \alpha_1 ENVDI_{it} + \alpha_2 ECNDI_{it} + \alpha_3 SDI_{it} + \alpha_4 Size_{it}^{11} + \alpha_5 CS_{it}^{11} + \alpha_6 Growth_{it}^{11} + \sum_{it}$ ....(4)

4. DATA ANALYSIS AND INTERPRETATION:

Dependent variable: As per the literature review, Sustainability reporting affects the operating efficiency of the business and it can even have the positive impact over financial performance with the increased social investing by the investors. **So this paper has considered ROA (operational measure) & ROE (Financial measure) as dependent variable**.

Independent Variables: To check the sustainability reporting impact on financial performance of the firm study has constructed **sustainability disclosure index** as per the GRI-G4 guidelines. And it is considered as the independent variable.

- Sustainability disclosure index [2] is also known as **ESG index** so here study has used **at first stage univariate analyses** to check overall impact of sustainability score on financial performance. And **in the second stage, multiple regressions is run to check individual impact of each of the** sustainability parameter on the financial performance. i.e, ECPDI, ENVDI & SOCDI.

Table -1 Overall Summary Statistics of Model-1&2

Model	R	R^2	Adjusted R^2	F-Statistics	Sig.F
Model-1(ROE-DV)	0.697777	0.456893	0.28165	2.37228	0.122151
Model-2(ROA-DV)	0.845852	0.715466	0.601653	6.286302	0.008537*

Predictor-(Constant) SRI & **Dependent Variable**: ROE &ROA **Control Variables**: D/E Ratio, Market Capitalization and Growth (Gross Revenue of firm)

From the Table-1 Model-1 above it is observed that there is 45% variation in the ROE of the business and after adjusting with statistically insignificant variables from the model there is still 28%variation found in ROE of the business and remaining is explained by other non-stochastic variables. Significant F-value 0.1221 is more than alpha 0.05 it means model is not statistically significant and **null hypothesis H1 is accepted i.e., there is not a significant impact of SDI on financial performance of the firm**.

From the table-1, Model-02 above it is inferred that there is a 71% variations in the ROA of the business and adjusted R^2 shows 0.60 shows that after adjusting insignificant variables there is a 60% variation in dependent variable ROA of the business and which is near to R^2 means model includes all the necessary variables and F-value 0.008 ,less than alpha 0.05 means model is statistically significant and **null hypothesis H2 is rejected .it can be inferred that sustainability related aspects (i.e.,EES) is influencing operating performance of the business.**

Table-2 Individual statistical significance of all explanatory variables-Model-1&2

Model	Independent Variable	Sustainability Reporting Index	Debt/Equity Ratio	Market Capitalization	Growth(Gross Revenue)
Model-1	Co-efficient β	-0.88497	-28.3813	2.3768	-2.4215
	P-Values	0.1914	0.1593	0.9943	0.9629
Model-2	Co-efficient β	-2.3989	-38.7262	-0.00002	0.00017
	P-Values	0.021734*	0.16882	0.596657	0.037156

*-It shows level of significance at 5% i.e., P〈 0.05 variable is Statistically Significant.

From the Table-02 above Model-01 it is inferred that there is a negative correlation between sustainability reporting and ROE & ROA of the business . individual statistical significance of the model described by p-value for model -02 it is inferred that Sustainability reporting index p-0.021734 is less than 0.05 so it is statistically significant and it is affecting operating performance of the business(ROA).

Table-3 **Overall Summary Statistics of Model -3&4**

Models	R	R^2	Adjusted R^2	F-Statistics	Sig.F
Model-3(ROE-DV)	0.708598	0.502111	0.128694	1.344639	0.3398
Model-4(ROA-DV)	0.848699	0.72029	0.510507	3.433507	0.055515*

Predictor-(Constant) Economic, environmental and Social disclosure index & **Dependent Variable**: ROA **Control Variables**: D/E Ratio, Market Capitalization and Growth (Gross Revenue of firm)

From the Table-03 Model-03 above it is observed that there is a 50%variation in the dependent variable ROE of the business with the taken predicators. Significance-F 0.3398 more than alpha @5% level of significance it is inferred that model is not statistically significant. **So null hypothesis H3 is accepted i.e., there is not a significant impact of sustainability related aspects (EES) and financial performance of the business (ROE).**

From the Table-03 Model-04 above it is observed that there is a 72% variation in the dependent variable ROA of the business with the taken predictors. Significance –F 0.0555 equal to alpha @5% level of significance it is inferred that model is statistically significant. **Hence null hypothesis H4 is rejected i.e., there is a significant impact of sustainability related aspects (EES) and Operating Performance of the business. (ROA)**

Table-4 Table Showing Individual Statistical Significance of all independent Variables

Independent Variable	Economic Disclosure index	Environmental Disclosure Index	Social Disclosure Index	Debt/Eq Ratio	Market Capitalization	Growth(Gross Revenue)
Co-efficient β (Model-03 ROE-DV)	-1.24259	1.573399	-1.48651	-22.7686	5.8485	-2.14395
P-Values	0.626549	0.76276	0.35863	0.365185	0.88176	0.97050
Co-efficient β(Model-04 ROA-DV)	-1.22625	-2.6200	-2.7145	-36.9908	-0.00002	0.0001
P-Value	0.7320	0.7213	0.2420	0.3001	0.6151	0.0662

From the Table-04 and Model-03 above it is observed that there is a linear relationship between Environmental disclosure index and ROE of the business. None of the independent variables are statistically significant.

From the Table-04 and Model-04 above it is observed that there is no linear relationship between any of the independent variables and none of the independent variables are statistically significant.

5. FINDINGS AND RECOMMENDATIONS:

- From the analysis of model-1&2 above it is found that sustainability reporting is more influencing to operating performance of the business as compared to financial.
- From the analysis of model-3&4 above individual dimensions of all the aspects of sustainability reporting, it is found that there is more variation in ROA(72%) as compared to ROE (50%)
- Out of three different aspects related to sustainability only environmental disclosure (Table-04) gives linear relationship with financial performance of the business not the operating performance. It means shareholders/investors get affected by firms' environmental related aspects and firm should take steps to improve their environmental related activities to boost up their financial performance and to reduce their cost of equity.
- It is recommended from the above findings that firm should improve their non-financial disclosure as it is having direct influence over their operating performance (ROA) [6] with 72%variations.And improvements in operating performance will automatically brings improvements in its Financial performance too.

6. LIMITATION & SCOPE FOR FUTURE RESEARCH:

The present study is based on only five firms and three years data future studies can be done with more sample size and more no. of years to generalize the results. Moreover present study has used ROA & ROE of the business as dependent variables future studies may incorporate other variable like EVA,MVA or enterprise value to check impact of sustainability reporting on valuation of the firm. Moreover study has considered only sustainability related aspects of non-financial disclosure future study can be performed with impact of ESG on financial performance. Moreover a primary research can be done to check how investors source and use the non-financial information for their decision-making.

7. CONCLUSION:

Indian businesses have started competing globally and stakeholders of the business even started giving weightage to non-financial performances of the firms in their dealings with the business. This has compelled companies to improve their non-financial performance and communicate the same via their sustainability and Business Responsibility Reporting. The objective of the present study was to check impact of sustainability reporting as per <GRI Framework>on financial and operating performance. The results of this study provide support to the view that there is a statistically significant relationship between SDI & Operating performance of the business. (Table-02/Model-02). Study add support to the view that out of three different aspects environmental related disclosure is statistically significant and affecting Financial performance of the business. It means investors/shareholders of the business are get affected with the environmental activity of the business and business should take steps to improvise the same. With the increasing socially responsible investing there will be improvise in the non-financial disclosure and performance of the business in India.

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Appendix-1

Corporate Sustainability disclosure index

Part	Category	Aspects	Indicators/ Items	Index Score received 2017-18	2016-17	2015-16
Governance & Engagement	Governance	13	27	24	24	24
	Stakeholder Engagement	1	1	1	1	1
	Total GE Score		**28**	**25**	**25**	**25**
Economic Disclosure	Economic Performance indicator	02	02	02	02	02
	Expenditure related to Operations, employee compensations, donations, other community investments, payment to capital providers and govt.	01	05	05	04	04
	Financial implications and other risks and opportunities for organization activities due to climate change.	01	01	01	01	01
	Financial assistant received from govt.	01	01	01	01	01
	Policy, Practices and proportion of spending on locally based suppliers at significant locations of operations.	02	02	02	02	02
	Total EC Score		**11**	**11**	**10**	**10**
Environmental Disclosure	Environmental vision, strategy	2	2	02	02	02
	Environmental Performance indicators	05	05	04	05	05
	Compliance and recognition/awards	02	02	02	02	01
	Environmental spending (Total environmental expenditure and investments by type)	01	02	00	00	00
	Total ED Score(EDS)		**11**	**08**	**09**	**08**
Social Performance Disclosure	Labor practices & Decent work performance indicators	06	06	04	06	06
	Human Rights Performance Indicators	09	09	04	08	09
	Society Performance Indicators	05	05	04	03	02
	Product Responsibility Performance Indicators	04	04	03	04	03
	Compliance and Recognition/Awards	01	01	01	01	01
	Total SPD Score		**24**	**16**	**22**	**21**