Corporate Sustainability Reporting and Firm’s Financial Performance in Emerging Markets

Wan Adibah Wan Ismail, Sazilah Mohd Saad, Nor Asma Lode, Nanik Kustiningsih

To Link this Article: http://dx.doi.org/10.6007/IJARBSS/v12-i1/11364

Received: 07 November 2021, Revised: 11 December 2021, Accepted: 25 December 2021

Published Online: 13 January 2022

In-Text Citation: (Ismail et al., 2022)


Copyright: © 2022 The Author(s)
Published by Human Resource Management Academic Research Society (www.hrmars.com)
This article is published under the Creative Commons Attribution (CC BY 4.0) license. Anyone may reproduce, distribute, translate and create derivative works of this article (for both commercial and non-commercial purposes), subject to full attribution to the original publication and authors. The full terms of this license may be seen at: http://creativecommons.org/licenses/by/4.0/legalcode

Vol. 12, No. 1, 2022, Pg. 396 – 407
http://hrmars.com/index.php/pages/detail/IJARBSS

Full Terms & Conditions of access and use can be found at http://hrmars.com/index.php/pages/detail/publication-ethics
Corporate Sustainability Reporting and Firm’s Financial Performance in Emerging Markets

Wan Adibah Wan Ismail  
Associate Professor Faculty of Accountancy Universiti Teknologi Mara Merbok, Kedah, Malaysia  
Email: wadibah@uitm.edu.my

Sazilah Mohd Saad  
Senior Lecturer Faculty of Accountancy Universiti Teknologi Mara Merbok, Kedah, Malaysia  
Email: sazilah@uitm.edu.my

Nor Asma Lode  
Associate Professor Tunku Puteri Intan Safinaz School of Accountancy Universiti Utara Malaysia Sintok, Malaysia  
Email: asma@uum.edu.my

Nanik Kustiningsih  
Doctoral Student Faculty of Economics and Business Universitas Airlangga Surabaya, Indonesia  
Email: nanik.kustiningsih-2017@feb.unair.ac.id

Abstract  
This paper investigates whether corporate sustainability reporting is associated with high firm performance in emerging markets. Using a sample of 24,029 firm-year observations from 14 emerging markets, including China, Egypt, Greece, Hungary, India, Malaysia, Pakistan, the Philippines, Poland, Russia, South Africa, Thailand, Turkey and the United Arab Emirates, we find firms with corporate sustainability reporting is associated with high firm performance. The results are robust even after including the firm-level controls of firm size, leverage, litigation risk, market-to-book ratio, firm age, industry-level control of market competition, and country-level control of the gross domestic product. The findings from this cross-country study provides significant implications for the regulators in promoting sustainability reporting and in assisting investors in making better decisions.

Keywords: Sustainability Reporting, Integrated Reporting, Stakeholders’ Interests, Firms Performance, Emerging Market
Introduction
Issues on corporate sustainability has become under spotlights in recent years, especially with the emergence of Covid-19 pandemic throughout the world. The pandemic has imposed great challenge to corporate business owners and managers due to restriction of human movement and business operations. Stakeholders and managers are not only concern on optimizing firms profitability and performance, but also on the disclosure of information of whether the business is sustainable and creating values to larger stakeholders. Thus, the disclosure relating to company’s sustainability in terms of its economic sustainability and competitive advantage, environmental sustainability and social communities’ sustainability are vital for companies to assess its potential financial and operational risks, manage their natural resources and capture timely business opportunities, which could translate into better financial performance.

Work considering the importance of sustainability reporting to the growth and performance of firms has a rich background. Sustainable reporting derives originally from corporate social responsibility reporting (CSR), now includes wider elements to cater the needs of information on firm’s value for various stakeholders. Global Reporting Initiative (GRI) was formed to help businesses, governments and other organizations understand and communicate their impacts on issues including environmental concerns, governance, human rights and corruption. GRI provides framework and standards for the preparation of sustainable reporting that enable third parties to assess environmental impact from the activities of the company and its supply chain. In essence, the reports complement corporate financial statements as it provides more communication about an organisation’s strategy, non-financial performance, governance, prospects, and external environment. (Al Hawaj & Buallay, 2021; Ismail et al., 2005). Melloni et al (2017), suggested that the firm’s financial and sustainability should communicate “concisely” about how a firm’s strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of sustainable value. Hence it will portray a “complete and balanced” report, i.e., broadly including all material matters, both positive and negative, in a balanced way.

Many claims that insights into the firm's business model to addressees both regular financial and nonfinancial reporting would increase firm performance (Busco et al., 2013; Alwi et al.,2013). In order to investigate whether these claims are true, this study examines the association between sustainable reporting and firms performance.

Literature Review
Studies on Sustainability Reporting
Extent studies has examined factors determining the inclusion of sustainability reporting in corporate reports (Bear et al., 2010; Da Silva Monteiro & Aíbar-Guzmán, 2010; Gallo & Christensen, 2011; Möller & Verbeeten, 2011; Dah & Jizi, 2016; Chang & McIlkenny, 2017; Anazonwu et al., 2018; Dissanayake et al., 2019; Kamarudin et al., 2012). The studies argue that factors such as the size of the company, corporate governance factors, and the intrinsic motivation of the management are among elements that influence the decision to implement the sustainable reporting. Other than the characteristics of a firm, other studies (Jiang & Fu, 2019; Manes-Rossi et al., 2018; Latridis, 2013) also found the evidence that the strength of corporate governance such as optimum board size and the representation of outside directors have positive associations with sustainability disclosure.

A strand of research examined the complexity and challenges behind the reasons of providing such reports. that the expected benefit of sustainability practices may not be apparent.
According to Kang et al (2010) there is a possibility that sustainability engagement may hinder optimal resource allocation, which could deter firms from their ultimate objective of maximizing the wealth of shareholders. This is due to the fact that in preparation of sustainability reports, firms need to face tensions in balancing the often divergent economic, social, and environmental goals. To a certain extent, firms may be lured towards ‘greenwashing’, as seen in the case of Volkswagen emission scandals, where incomplete or false information was intentionally provided to legitimately appear sustainability-oriented in order to gain economic benefits (Kamarudin et al., 2021). In addition, a study by Chen et al (2015) showed that some firms tended to apply for repetitive disclosures in order to suppress other disclosures, providing evidence for the manipulative power of management regarding these reports.

Previous studies on sustainability reporting have examined the benefit of sustainability practices and value creation. The studies found that commitment towards sustainable reports allows firms to gain competitive advantage (Hart & Milstein, 2003; Porter & Kramer, 2011) from the efficient allocation of firm-specific resources and capabilities that are inimitable by competitors (Barney, 1991; Rumelt, 1987). It is also found that embedding corporate sustainability agenda stimulates innovation (Porter & Van der Linde, 1995), motivates employees to exert greater effort (Fauver et al., 2018) and strengthens a firm’s resilience to external shocks (Desjardine et al., 2019). Friede et al (2015); Platonova et al (2018) also suggest that commitment towards sustainability is value-enhancing and thus could positively impacts the financial performance of firms.

**Hypothesis Development**

Several studies have proposed that sustainability reporting disclosures would increase business effectiveness and create value (Zamfir et al., 2017; Ouvrard et al., 2020; Nosratabadi et al., 2020). The evidence of the relationship between corporate sustainability reporting and financial performance, however, is mixed. There was some evidence of support for sustainability reporting, for example, and costly corporate social responsibility initiatives would divert managers from maximizing shareholder wealth (Liang & Renneboog, 2016). In contrast, many studies perceived that corporate sustainability is essential in mitigating risk, especially the negative consequences resulting from irresponsible acts of a firm to society and the environment (Latridis, 2013). Besides, sustainability reporting signals the business conduct to users (Sweeney & Coughlan, 2008; McWilliams & Siegel; 2000; Hu et al., 2020). Thus, for example, corporate social responsibility strategies could positively be associated with business performance.

Al Hawaj & Buallay (2021) added a new perspective to the sustainability reporting on integrating macroeconomic data. For ten years, from 2008 to 2017, data was collected from 3,000 companies in 80 different countries (cumulatively 23,738 observations). The empirical data show that there are disparities in the influence of sustainability reporting (ESG) on a firm’s operational performance (ROA), financial performance (ROE), and market performance (TQ) across the seven sectors. This study offers a baseline for organisations intending to adopt sustainability reporting by contributing to the literature of sustainability accounting by providing a systematic depiction of cross-sectorial ESG reporting.

On the positive side, many studies have found the benefits of sustainability reporting. In Italy, for example, a study on multinational companies and private and public organizations suggested that the sustainability risk disclosure positively influenced by sustainability experience and international presence but was not affected by the presence of external insurance (Truant et al., 2017). Thus, by disclosing environmental information, experts are
continually looking for new ways to protect the reputation of and benefits to stakeholders, improve eco-performance (Yu et al., 2018; Orlitzky & Swanson, 2012; Ismail et al., 2012), or explore various existing relationships between sustainability reporting and the disclosure of ethical–social–environmental risks (Truant et al., 2017, Buchan, 2012; Grieco, 2015; Cameron, 2010; Costa & Pesci, 2016; Bice, 2015; Schneider & Meins, 2012, Wan Ismail et al., 2005). Sustainable reporting also leads to better performance as the concerns for environment and creation of values would improve corporate reputation and thus gain positive implications. However, there are conflicting conclusions in the literature in the context of corporate reputation and sustainability reporting (Landau et al., (2020); Lozano et al., 2016; Kang & Liu, 2014; Heinze et al., 1999; Amin et al., 2013). On one hand, corporate responsibility commitments could positively impact productivity through proactive communication and motivating purchase intention (Heinze et al., 1999; Cupertino et al., 2019; Dang et al., 2018). Besides, sustainable reporting could tarnish corporate reputation if negative involvements are revealed. A study by Ceulemans et al (2015) also found that the benefit of sustainable reporting is mixed. From a sample of 64 educational institutions around the world, the study found that 23 demonstrated positive aspects based on the internal motivations expressed through the awareness of sustainability and improvement of the communication with their stakeholders. Nonetheless, there are also the negative impacts which is due to the lack of inclusion of the material effects in the reports, the lack of external involvement of the stakeholders, the lack of implementation of sustainability reporting in the operation (Ceulemans et al., 2015).

Based on the argument that sustainable reporting leads to value creation, and enhanced firms performance, the following hypothesis is tested:

Hypothesis 1 (H1): Sustainability reporting is positively associated with financial performance.

Research Methodology

This study is a quantitative in nature to examine the relationship between variables. The research design used in this study is correlational research that uses a Weighted Least Squares regression on equation using the inverse number of observations in each country as a weight. (Salkind, 2014).

Sample Selection

The data cover the period 2011–2018 obtained from various sources. We extracted the financial data from Thomson Reuters Fundamentals, while the country-level data were extracted from annual World Economic Forum reports and the World Bank database. We deleted all missing observations. Our final sample consists of 24,029 firm-year observations from 14 countries: China, Egypt, Greece, Hungary, India, Malaysia, Pakistan, the Philippines, Poland, Russia, South Africa, Thailand, Turkey and United Arab Emirates. We winsorised the observations that fell in the top and bottom one per cent of all continuous variables to mitigate the influence of outliers.

Regression Model

As our number of observations varied substantially across countries, we employ a Weighted Least Squares regression on equation (1) using the inverse number of observations in each country as a weight. We followed the approach in prior studies (Jaggi & Low, 2011; Lang & Sul, 2014) to ensure that the results are not biased by more heavily represented countries.
\[ ROA = \alpha_0 + \beta_1 SUST + \beta_2 SIZE + \beta_3 LEV + \beta_4 LIT + \beta_5 MTB + \beta_6 COMP + \beta_7 AGE + \beta_8 LGDP + \theta_{t, n} \text{Fixed-effects}_t + \varepsilon_{it} \] (1)

Where ROA is the return on assets; SUST is a dummy variable that takes value 1 if the company discloses sustainable reporting, otherwise 0; SIZE is the natural logarithm of total assets; LEV is the ratio of total liabilities over the total assets; LIT is a dummy variable of high-litigation industries, classified as 1 if the SIC codes were between 2833–2836, 3570–3577, 3600–3674, 5200–5961 and 7370–7370, otherwise 0 (Ashbaugh & LaFond, 2003); MTB is the ratio of market-to-book value; COMP is the proxy for industry competition measured as the sum of the squares of the market shares (calculated based on total assets) of all the firms in five industries classification of Fama and French (1997) has multiplied with negative one; SARS is the index of strength of the accounting and reporting standards issued by the World Economic Forum is higher than the mean value; LGDP is the natural logarithm of gross domestic product per capita in U.S. dollars from the World Bank; and Fixed-effects are controls for industry and year effects.

**Discussion of Results**

**Descriptive Statistics**

Table 1 presents descriptive statistics for firm-level variables and country-level variables. The result shows that the average ROA is 0.046, with values ranging from -0.498 and 0.374. The mean value for SUST is 0.052, indicating that 5.2 per cent of the sample reports sustainable reporting. For the control variables, the mean for SIZE is 18.908 with a range between 13.313 and 24.455. The variable LEV has a mean value of 0.231 with a value ranging from 0.000 and 1.146. A dummy for LIT has a mean value of 0.144, indicating that 14.4 per cent of the sample are from high litigious industries. Other variables, MTB, COMP, and AGE, have mean values of 2.218, -0.087, and 23.317, respectively. The mean value for LIT is 0.181, indicating that 18.1% of the sample are from highly litigious industry.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>Std. Dev.</th>
<th>Min</th>
<th>Max</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>0.046</td>
<td>0.103</td>
<td>-0.498</td>
<td>0.374</td>
</tr>
<tr>
<td>SUST</td>
<td>0.052</td>
<td>0.222</td>
<td>0.000</td>
<td>1.000</td>
</tr>
<tr>
<td>SIZE</td>
<td>18.908</td>
<td>2.077</td>
<td>13.313</td>
<td>24.455</td>
</tr>
<tr>
<td>LEV</td>
<td>0.231</td>
<td>0.217</td>
<td>0.000</td>
<td>1.146</td>
</tr>
<tr>
<td>LIT</td>
<td>0.144</td>
<td>0.351</td>
<td>0.000</td>
<td>1.000</td>
</tr>
<tr>
<td>MTB</td>
<td>2.218</td>
<td>3.829</td>
<td>-2.323</td>
<td>32.950</td>
</tr>
<tr>
<td>COMP</td>
<td>-0.087</td>
<td>0.092</td>
<td>-0.979</td>
<td>-0.013</td>
</tr>
<tr>
<td>AGE</td>
<td>23.317</td>
<td>14.134</td>
<td>4.000</td>
<td>57.000</td>
</tr>
<tr>
<td>SARS</td>
<td>4.855</td>
<td>0.474</td>
<td>3.766</td>
<td>6.577</td>
</tr>
<tr>
<td>LGDP</td>
<td>7.232</td>
<td>1.293</td>
<td>5.164</td>
<td>9.015</td>
</tr>
</tbody>
</table>

Table 2 presents simple correlations among the variables. The result shows that ROA is positively correlated with several variables, which are SUST, SIZE, LIT, MTB, COMP, AGE and LGDP. This is reasonable as the variables are expected to contribute towards firms
performance. We also observed that LEV has negative relationship with ROA, consistent with the expectation that highly leveraged firms would have higher cost of capital, which could possibly decrease firms’ profitability. More importantly, the correlation matrix also shows that the correlations between the independent variables are relatively low, hence suggesting that multicollinearity is unlikely to be an issue in the multivariate regression analyses.

<table>
<thead>
<tr>
<th>Table 2: Correlation Matrix</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td>ROA</td>
</tr>
<tr>
<td>SUST</td>
</tr>
<tr>
<td>SIZE</td>
</tr>
<tr>
<td>LEV</td>
</tr>
<tr>
<td>LIT</td>
</tr>
<tr>
<td>MTB</td>
</tr>
<tr>
<td>COMP</td>
</tr>
<tr>
<td>AGE</td>
</tr>
<tr>
<td>SARS</td>
</tr>
<tr>
<td>LGDP</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>MTB</th>
<th>COMP</th>
<th>AGE</th>
<th>SARS</th>
<th>LGDP</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MtB</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>COMP</td>
<td>0.027***</td>
<td>1.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>AGE</td>
<td>-0.042***</td>
<td>0.040***</td>
<td>1.000</td>
<td></td>
</tr>
<tr>
<td>SARS</td>
<td>-0.045***</td>
<td>-0.024***</td>
<td>0.144***</td>
<td>1.000</td>
</tr>
<tr>
<td>LGDP</td>
<td>0.149***</td>
<td>0.368***</td>
<td>-0.256***</td>
<td>-0.405***</td>
</tr>
</tbody>
</table>

Asterisks denote statistical significance at the 1% (***) or 5% (**), or 10% (*) levels, respectively.

Main Results

Table 3 presents the regression estimates for the effect of sustainability reporting on firm performance.

<table>
<thead>
<tr>
<th>Table 3: Regression Estimates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>SUST</td>
</tr>
<tr>
<td>SIZE</td>
</tr>
<tr>
<td>LEV</td>
</tr>
<tr>
<td>LIT</td>
</tr>
<tr>
<td>MTB</td>
</tr>
<tr>
<td>COMP</td>
</tr>
<tr>
<td>AGE</td>
</tr>
<tr>
<td>SARS</td>
</tr>
<tr>
<td>LGDP</td>
</tr>
<tr>
<td>Fixed Effects</td>
</tr>
<tr>
<td>Obs</td>
</tr>
<tr>
<td>Adj R-squared</td>
</tr>
<tr>
<td>F-stat</td>
</tr>
</tbody>
</table>

Asterisks denote statistical significance at the 1% (***) or 5% (**), or 10% (*) levels, respectively.
We find that the coefficient for SUST is positive and significant, showing that in sustainability reporting is associated with high firm performance. This finding supports the notion that firm with high financial performance have greater tendency to produce sustainability reporting compared to firms with poor financial performance.

The regression estimates also show that the coefficient of the control variables, which are SIZE, MTB, COMP, AGE, and LGDP are positively significant (p<0.01), suggesting that ROA is associated with these variables, consistent with the evidence from prior studies. We also find the coefficient for LEV, LIT and LGDP are positively significant (p<0.01), suggesting that lower financial performance in firms with high-risk firms, high litigious firms and in countries with high income per capita.

Conclusion
This research tests and finds that sustainability reporting results in high financial performance in emerging market. This finding is consistent with prior studies that sustainability reporting disclosure would increase firm’s profit through greater value creation (Hu et al., 2020; Truant et al., 2017; Yu et al., 2018), greater competitive advantage (Hart & Milstein, 2003; Porter & Kramer, 2011), more efficient allocation of firm’s resources (Barney, 1991; Rumelt, 1987), greater stimulation of innovation (Porter & Van der Linde, 1995), better employees’ motivation (Fauver et al., 2018) and stronger resilient to external shocks (Desjardine et al., 2019). Investors could benefit from sustainability reporting as it helps protect shareholders’ investment by promoting high-quality information. Our study provides valuable insights to investors and policymakers, especially in emerging markets, in terms of promoting sustainability reporting and providing incentive to disclosing firms. Going forward, we encourage more research on sustainability reporting and incorporating other institutional variables such as investor protection and culture.

Acknowledgments
The authors thank the editor and anonymous reviewers of the International Journal of Academic Research in Business and Social Science for insightful and constructive comments. The research is financially supported by the UITM-UNAIR Matching Grant No 100-TNCPI/INT 16/6/2 (027/2020).

References
working capital accruals. Working paper, University of Wisconsin.


https://doi.org/10.1080/14615517.2014.983710


Landau, A., Rochell, J., Klein, C., & Zwergel, B. (2020). Integrated reporting of environmental, social, and governance and financial data: Does the market value integrated


