

Exploring the Relationship of Corporate Sustainability Reporting, Its Quality, and Firms' Market Values: Evidence from the Philippines' Most Actively Traded Publicly-Listed Companies

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Abstract - In recent years, stakeholders have become more conscious of the impact of businesses on the economy, environment and society. In effect, companies around the globe have adopted sustainability reporting to assuage stakeholders' concerns through the disclosure of relevant information. The agency theory, legitimization theory and signal theory suggest that sustainability reporting has an incremental effect on firms' market values. Hence, the study endeavored to probe on whether a significant relationship exists between the issuance of sustainability reports prepared using the Global Reporting Initiative (GRI) Guidelines, and the market values of the 93 most actively traded companies comprising the Philippine Stock Exchange sector indices. A regression analysis was performed using a modified Ohlson model to test the significance of the relationships among the variables. For companies with sustainability reports, the study further examined whether better quality reporting permits stronger linkage with firms' market values. Content analysis was conducted to assign scores to the reports based on the specific disclosures of the GRI Guidelines. Results revealed a significant positive relationship between the issuance of sustainability reports and firms' market values. However, there is a weak association between quality reporting and firms' market values. The study concludes that publicly-listed companies can merit from the practice of sustainability reporting as it continues to gain traction in the Philippines.

Keywords - sustainability, sustainability report, sustainability reporting, GRI standard, Ohlson model

I. INTRODUCTION

The heightened public awareness and attention on economic growth, environmental stewardship, and social equity have shaped the evolution of what is now known as sustainability reporting (Elkington, 1999 as cited in Brown, de Jong, & Lessidrenska, 2009). Evolving from non-financial reporting and corporate social responsibility, sustainability reporting has seen rapid adoption by major companies in recent years. A survey conducted in 2017 has revealed a substantial growth in the number of companies issuing sustainability reports. Among the 250 Fortune Global companies, the percentage of companies issuing such reports has increased from 35% in 1999 to 93% in 2017. Likewise, among the 4,900 companies that ranked within their respective countries' top 100 based on revenue, adoption of sustainability reporting has increased from 12% in 1993 to 75% in 2017.

In the Philippines, sustainability reporting is still relatively new, with only less than 22% of publicly listed companies issuing sustainability reports in 2017 (KPMG, 2017). On February 12, 2019, the Securities and Exchange Commission (SEC) issued Memorandum Circular No. 4-2014 or the Sustainability Reporting Guidelines for Publicly Listed Companies, requiring all publicly listed companies to attach sustainability reports to their annual reports for the financial year 2019 and onwards. The Guidelines shall be adopted on a "comply or explain" approach for the first three years of implementation. Hence, the number of companies issuing sustainability reports is expected to rise in the following years.

Due to the multidimensional and complex nature of sustainability, several standards have been promulgated to assist firms in measuring and communicating their sustainability performance to stakeholders. Among these standards, the most prominent is the General Reporting Initiative Guidelines

developed by the General Reporting Initiative (GRI), a non-profit international organization developed by the Coalition for Environmentally Responsible Economies (CERES) and the United Nations Environment Programme (UNEP) (GRI 2009B). The first set of guidelines was published in June 2000 and has since been improved on numerous times. The latest set was launched in October 2016 and is known as the GRI Standard.

As sustainability reporting gains popularity, its influence on market valuation and financial performance has become an extensively debated subject in literature. Data from interviews and surveys provide evidence that sustainability information is desired by investors, implying that the information is relevant in investment decisions (Solomon, J. F., & Solomon, A., 2006). A study of Canadian companies listed in the Toronto Stock Exchange suggests that investors positively value sustainability reporting (Berthelot, Coulmont, & Serret, 2012). The same finding is echoed in a study by Kuzey & Uyar (2017) of Turkish publicly traded companies at Borsa Istanbul. Likewise, Reddy & Gordon (2010) claims that sustainability reporting is statistically significant in explaining abnormal stock returns of Australian publicly listed entities. Another study of Australian companies reveals a significant negative association between sustainability reporting and cost of equity (Bachoo, Tan & Wilson, 2013). Similarly, a study on Greek firms suggests a positive correlation between stock returns and corporate social responsibility performance (Karagiorgos, 2010). Khaveh, Seyed, Yousefi, & Haque (2012), in their study of Singaporean companies, have found that there is a significant positive relationship between revenue and share price and sustainability reporting. These studies suggest that investors place a premium on companies that practice sustainability reporting.

While investors following ethical or socially responsible investing are often thought to be foregoing economic returns for

been entirely voluntary up until February 12, 2019 when SEC issued Memorandum Circular No. 4-2019 requiring all publicly-listed companies to submit sustainability reports for the financial year 2019 and onwards. However, since the SEC follows a “comply-or-explain” approach, companies still have the leeway not to disclose sustainability information.

Table 3
Sustainability Reporting by Sector

| | Actively Traded Companies in PSE | Actively Traded Companies with Sustainability Reporting | Percentage of Companies with Sustainability Reporting |
|----------------|----------------------------------|---|---|
| Financials | 9 | 4 | 44.44% |
| Holding Firms | 14 | 4 | 28.57% |
| Mining and Oil | 7 | 2 | 28.57% |
| Services | 22 | 4 | 18.18% |
| Industrial | 24 | 4 | 16.67% |
| Property | 17 | 1 | 5.88% |
| Total | 93 | 19 | 20.43% |

The sustainability reports issued by the 19 companies were scored based on the specific disclosures provided in the GRI Standard. Shown in Table 4 are the average scores and standard deviations of the sectors per category (economic, environmental, and social). Among the six sectors, the Industrial sector, which is the largest sector based on market capitalization, registered the highest total average score of 104/340 or 31%. Narrowing down to the different categories, the Industrial sector also obtained the highest average score in both economic and environmental dimensions and the second highest average score in the social dimension.

Table 4
Sustainability Reporting Score per Sector

| Sector | Economic | | Environmental | | Social | | Total Score | |
|----------------|----------|-----------|---------------|-----------|---------|-----------|-------------|-----------|
| | Ave | Std. Dev. | Ave | Std. Dev. | Ave | Std. Dev. | Ave | Std. Dev. |
| Industrial | 20 (38) | 5 (51) | 11 (45) | 3 (33) | 8 (20) | 104 (31) | 16 (16) | |
| Mining and Oil | 13 (25) | 6 (35) | 2 (29) | 2 (31) | 5 (18) | 5 (78) | 23 (8) | |
| Services | 10 (19) | 6 (22) | 14 (39) | 14 (39) | 27 (71) | 21 (21) | 47 (47) | |
| Holding Firms | 11 (21) | 7 (24) | 20 (25) | 22 (33) | 10 (58) | 58 (17) | 40 (40) | |
| Financials | 13 (25) | 3 (11) | 9 (9) | 2 (21) | 13 (13) | 6 (45) | 13 (10) | |
| Property | 4 (8) | N/A | 8 (7) | N/A | 20 (12) | N/A | 32 (9) | N/A |
| Overall | 13 (25) | 6 (27) | 22 (22) | 20 (29) | 17 (17) | 68 (20) | 35 (35) | |

Note: The numbers in parentheses represent the percentage of maximum total score of 340

While there are several subsectors under the Industrial sector, the four companies that had issued sustainability reports all belong to the Electricity, Energy, and Power & Water subsector. These companies garnered high scores in the economic category due to their thorough reporting on the direct economic value created to different stakeholders; risks, financial implications, and opportunities modelled by climate change on their organization's activities; and important indirect economic impacts which include significant infrastructure investments, services supported and positive and negative influence on local communities. These companies also registered high scores in the environmental category due to their detailed disclosures on water withdrawal, energy consumption, habitats protected or restored, waste disposal, and greenhouse gas emissions. These results can be explained from the perspective of legitimization whereby the Industrial sector aims to project a positive image in response to high levels of public

apprehension and scrutiny.

Meanwhile, the Services sector received the highest average score in the social category owing to the extensive disclosures on the hiring and turnover of employees, benefits provided, trainings conducted and local community engagement. This can mean that the Services sector places a high priority on people management and development.

The average total score of all the companies issuing sustainability reports is only 68/340 or 20%. This implies that the quality of sustainability reporting needs to be improved considerably in order to meet international standards. Moreover, there is a huge variation in the quality of reports among companies in the same sector and across sectors as indicated by the high standard deviations.

After looking into the sustainability reports quality scores, a correlation test was conducted to establish the relationship between the variables used in the modified Ohlson model. Table 5 shows the correlation results.

Table 5
Correlation Matrix of the Variables

| | MV _{it+5} | BV _{it} | EARN _{it} | SR _{it} | SRO _{it} |
|--------------------|--------------------|------------------|--------------------|------------------|-------------------|
| MV _{it+5} | 1.0000 | | | | |
| BV _{it} | 0.6480 | 1.0000 | | | |
| EARN _{it} | 0.7100 | 0.8404 | 1.0000 | | |
| SR _{it} | 0.3823 | 0.2334 | 0.3148 | 1.0000 | |
| SRO _{it} | 0.2290 | 0.1603 | 0.1777 | 0.1777 | 1.0000 |

Table 5 reveals that all the variables have positive correlations. The correlations of the issuance of sustainability reports and quality of sustainability reports with market value registered values higher than 0.2. Furthermore, book value and earnings correlate strongly with market value at 0.64 and 0.71, respectively. These results indicate a possibility that the issuance and quality of sustainability reports may affect firms' market values alongside book values and earnings.

After ascertaining the correlation of the different variables, a regression analysis was conducted.

Table 6
Regression Analysis: Market Value to Book Value, Earnings and Issuance of Sustainability Report

| Term | Coefficient | P-Value |
|--------------------------------------|----------------|---------|
| Constant | 6,412,738,463 | 0.716 |
| Book Value | 0.377 | 0.146 |
| Earnings | 8,949 | 0.001 |
| Sustainability report issuance | 87,790,858,387 | 0.018 |
| Model Summary: | | |
| R-squared (Coefficient of Variation) | 54.31% | |

Table 6 reveals that earnings and the issuance of sustainability reports registered P-values less than the level of significance (0.05). Thus, there is sufficient evidence to show that companies issuing sustainability reports tend to have higher market values than those that do not. Book value, on the other hand, registered a p-value more than 0.05; hence, on the onset of the study, there is not yet enough evidence to prove its significant relationship with market value. Moreover, the coefficient of variation (R-square) was computed to be 54.31%. This indicates that most of the variations of the market value can be accounted for from the variations of the three variables of interest. The other 45.69% of the explanatory factors can be explained by other factors external to the interest of this research and can be a good take off for future research endeavours.

The outcomes of the regression analysis were then

incorporated to Model 1 to test the first hypothesis (H₁). Hence, the equation below.

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$$\begin{aligned}
 \text{Model 1} \\
 MV_{it+5} &= \alpha_0 + \alpha_1 BV_{it} + \alpha_2 EARN_{it} + \alpha_3 SR_{it} + \epsilon_{it} \\
 MV_{it+5} &= 6,412,738,463 + 0.377BV_{it} + 8,949EARN_{it} + \\
 & 87,790,858,387SR_{it}
 \end{aligned}$$

From the general equation, as depicted by Model 1, categorical predictor equations were derived to show further the difference in market value between companies issuing sustainability reports and those that do not.

| | |
|-----------------------------------|--|
| Without Sustainability Report (0) | MV = 6,412,738,463 + 0.377BV + 8,949 EARN |
| With Sustainability Report (1) | MV = 94,203,596,850 + 0.377BV + 8,949 EARN |

The results concur with the signal theory whereby investors and other stakeholders ascribe a premium to companies that voluntarily report on sustainability. Consequently, this leads to the acceptance of the first alternative hypothesis that companies with sustainability reports have significantly higher market values.

After examining the relationship of issuance of sustainability reports with market value, a further investigation of the association between the reporting quality and firm's value was conducted

Table 7
Regression Analysis: Market Value to Quality of Sustainability Report

| Term | Coefficient | P-Value |
|--------------------------------------|---------------|---------|
| Constant | 8,415,907,853 | 0.589 |
| Earnings | 12.65 | 0.000 |
| Sustainability report scoring | 649,040,227 | 0.160 |
| Model Summary: | | |
| R-squared (Coefficient of Variation) | 51.49% | |

The results of the regression analysis were then incorporated to Model 2 to test the second hypothesis (H₂). Hence, the equation below.

$$\begin{aligned}
 \text{Model 2} \\
 MV_{it+5} &= \alpha_0 + \alpha_1 BV_{it} + \alpha_2 EARN_{it} + \alpha_3 SRO_{it} + \epsilon_{it} \\
 MV_{it+5} &= 8,415,907,853 + 0.332BV_{it} + 12.65EARN_{it} + \\
 & 64,904,022,7SR_{it}
 \end{aligned}$$

As shown in Table 7, the P-value of the quality of sustainability reports is more than 0.05, denoting a positive but insignificant relationship with market value. On the other hand, the coefficient of variation registered at 51.49%, which is lower than that of the first model. Hence, there is no sufficient evidence to show that companies with better quality reporting tend to have higher market values. Thus, the second alternative hypothesis is rejected.

The findings suggest that the issuance of sustainability reports has a significant positive relationship with firms' market values, signifying that investors appreciate the value of sustainability reporting. However, there is a weak association between the quality of sustainability reports and firms' market values. This can be attributed to the lack of legislation regarding sustainability reporting or even the seemingly lack of awareness of various stakeholders. Moreover, stakeholders may have appreciated the issuance of sustainability reports but may have

encountered difficulties in measuring and comparing the sustainability performance of companies based on the sustainability reports alone. Such difficulties may be due to the qualitative features of sustainability, non-compliance with GRI protocols, indicator contingency, ambiguous or incomplete information, data heterogeneity, and report opacity (Boiral & Henri, 2017). Amir (2012) posits that the manual process of analyzing sustainability reports is becoming obsolete and tedious, and the development of a tool or software that can significantly ease the process is imperative.

IV. CONCLUSIONS

The growing concern of various stakeholders on the management of sustainability by companies has led to the widespread promulgation of sustainability reporting in recent years. The research shows that there is a significant positive relationship between the issuance of sustainability reports and firms' market values, implying that investors appreciate the value of sustainability reporting. However, there is a weak association between the quality of sustainability reports and firms' market values, which may be due to the inadequate adoption of sustainability reporting, weak rules and regulations, and the lack of awareness of various stakeholders. In light of these findings, the study concludes that publicly listed companies can merit from the practice of sustainability reporting as it continues to gain traction in the Philippines.

V. RECOMMENDATIONS

The results of the study highlight the need for Philippine publicly listed companies to considerably improve their reporting skills in order to meet international standards. Furthermore, the results of the study may guide regulators in developing a comprehensive set of industry-specific sustainability metrics to facilitate benchmarking by companies and to assist investors in making investment decisions. Recognizing the limitations inherent in this study, future studies are recommended to consider a larger sample size, a wider timeframe, and more sustainability reporting frameworks in order to fully capture the relationship between sustainability reporting and firms' market values.

ABOUT THE RESEARCHERS

All the researchers were affiliated with the University of San Jose-Recoletos during the conduct of the study. Sarah M. Balisacan is a full-time Accounting Instructor. Hannah Joyce R. Miranda, John Karlo P. Caminero, and Rhea Angelica D. Semblante were Bachelor of Science in Accountancy students and have since graduated last October 2019. The research was initially undertaken in compliance with the requirements of the course Accounting 219 Research Synthesis.

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APPENDIX

Appendix A
Summary of Sustainability Report Scores

| | Economic | Environmental | Social | Total |
|-----------------------|----------|---------------|--------|-------|
| Mining and Oil | | | | |
| Company A | 17 | 33 | 34 | 84 |
| Company B | 9 | 36 | 27 | 72 |
| Industrial | | | | |
| Company C | 23 | 55 | 33 | 111 |
| Company D | 14 | 46 | 24 | 84 |
| Company E | 25 | 65 | 31 | 121 |
| Company F | 16 | 39 | 44 | 99 |
| Holding Firms | | | | |
| Company G | 21 | 62 | 34 | 117 |
| Company H | 10 | 12 | 17 | 39 |
| Company I | 6 | 14 | 27 | 47 |
| Company J | 8 | 9 | 11 | 28 |
| Property | | | | |
| Company K | 4 | 8 | 20 | 32 |
| Financials | | | | |
| Company L | 14 | 12 | 20 | 46 |
| Company M | 12 | 12 | 21 | 45 |
| Company N | 16 | 11 | 29 | 56 |
| Company O | 8 | 8 | 15 | 31 |
| Services | | | | |
| Company P | 4 | 6 | 20 | 30 |
| Company Q | 7 | 19 | 24 | 50 |
| Company R | 12 | 20 | 34 | 66 |
| Company S | 18 | 41 | 79 | 138 |