Investment issues of agricultural enterprises in the context the development ESG agenda

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Abstract. This article examines the need for disclosure of non-financial information in agricultural organizations. The authors use the comparison method to prove the need to disclose information in the social, environmental and corporate governance spheres. The importance of dividing into these areas is explained by the ESG agenda. The authors of the article emphasize that there is a sufficient number of studies confirming the positive impact of disclosure of non-financial information on various companies. It was noted both the impact of non-financial disclosures on the financial performance of companies (such as return on assets and return on equity), and the increase in the investment attractiveness of organizations, resulting in stock prices raise. In most cases, this can be explained by current trends, according to which solving environmental problems is a key task. As a result of the analysis, it was concluded that companies need to follow trends and disclose significant facts not only about the financial component of their activities, but also about the non-financial – how they affect the environment and society.

1 Introduction

Due to the Sustainable Development Goals published by the UN in 2015, as well as to the new agenda of Industry 5.0, attention to the environment and ecology of the entire planet has increased. To track the actions that companies perform to preserve nature, the principles of non-financial reporting on sustainable development have been created. Also the ESG agenda has become widespread. In a broad sense, this is the sustainable development of commercial activities, which is based on the following principles: responsible attitude to the environment (E – environmental); high social responsibility (S – social); high quality of corporate governance (G – governance). Its main idea is to disclose non-financial information of companies about their impact on the environment and society around us. These circumstances create completely new conditions for the business development of agricultural companies. It is possible to identify the risks that they face taking into account the new requirements of the company: new requirements for attracting investments, problems in exporting products, mandatory requirements for the implementation of measures aimed at countering the destructive effects of companies in relation to this ecosystem.

The risks of investing in new conditions should be considered from two points of view: access to cheaper investment resources, on the one hand, and the complication of access to...
investment resources in general, companies ignoring the requirements of the modern agenda, on the other hand.

In 2020, Ernst & Young (EY) conducted a survey among institutional investors—insurance and investment companies, pension and charitable foundations. As a result, according to RBC, 98% of respondents stated that they strictly monitor the company's ESG rating. Moreover, if earlier the approach of inverters based on ESG principles was based on ethical ideas; now the materiality of ESG, quantitative disclosure of information and the impact of the approaches used by companies on the future capitalization of companies and the ability to provide better performance adjusted for risk prevail.

Thus, non-disclosure or poor-quality disclosure of information in non-financial statements will inevitably lead companies to an objective decrease in their investment attractiveness, taking into account the developed model estimates.

On the other hand, special tools are being created in all countries to invest in companies implementing ESG practices. In many countries, there are special programs under which banks have the opportunity to provide loans for the development of agriculture, in particular, in accordance with the principles of sustainable development. The standards for issuing securities make the conditions for issuing "green" and social bonds less strict.

The same trend is developing in the Russian Federation. In 2022, the Bank of Russia amended the Securities Issuance Standards, according to which companies can issue new types of bonds: adaptation bonds, bonds related to sustainable development goals, climate transition bonds. Russian companies have received an additional opportunity to attract financing for the transformation of their business, taking into account the Sustainable Development Goals and national goals for the transition to a low-greenhouse gas economy.

However, in order to attract investment resources within the framework of these projects, companies must provide detailed and accurate information in non-financial reporting. In addition, the model methodology of ESG ratings developed by the Bank of Russia 2023 includes specific indicators (for example, on the reclamation of agricultural land).

The second important aspect of agricultural companies’ possible losses risk, taking into account ESG factors, is the reduction of export opportunities. This is due to the introduction of environmental taxes in different countries for exporters whose products are manufactured in violation of the requirements for environmental friendliness and carbon footprint. Currently, the potential for export reductions for Russian agricultural producers is estimated by experts to be within 20%, which is significantly lower than, for example, for oil and gas companies.

However, it should be borne in mind that standard indicators of profitability and capital intensity make agricultural companies much more sensitive to such losses. At the same time, the requirements for the implementation of eco-restoring measures will require additional investments.

Thus, in the current conditions, agricultural companies operating without taking into account the requirements of the ESG agenda may face a simultaneous increase in investment needs due to stricter environmental requirements and a reduction in demand for products. At the same time, non-compliance with the requirements of the company's environmental impact assessment deprives it of preferential access to cheap investment resources, special ESG financial instruments and loans that will be used by similar companies that comply with the necessary requirements and disclose them in non-financial statements.

Secondly, the investment attractiveness of such a company is reduced due to the embedding of ESG factors in investment rating models.
2 Materials and methods

This paper is based on a review of existing studies about the impact of non-financial information disclosure on the Russian companies’ financial performance. The first stage is based on the consideration of the agriculture features as a separate industry and the necessity to disclose non-financial information to increase the investment attractiveness of organizations. The second stage is the review of the existing practice of non-financial information disclosure and ESG indicators based on the Russian companies’ statistics.

3 Results

The following literature review is intended to give a certain background to the study on the relationship of non-financial information disclosure to the financial performance of the company. As for the literature review on the subject of ESG, in recent years this topic has been quite popular in scientific circles. It caused a lot of doubts and additional questions due to the lack of definite answers from the experts. Most studies and articles can be divided into several categories. Thus, 4 categories of the most popular topics of publications can be distinguished:

• the relationship between financial and non-financial reporting (ESG)
• the concept and methods of ESG integration
• the level of investor satisfaction with the quality of ESG information disclosure.
• increased interest is also paid to the impact of COVID-19 on the non-financial reporting disclosures

In addition, many other studies have examined the impact of ESG participation on corporate behavior and its market performance from several perspectives, including corporate value, stock price collapse risk, revenue management, individual risk, and green innovation.

Both the negative and positive effects of ESG usage on the economics are discussed. Firstly, speaking about the positive impact of ESG, studies claim that firms take on social responsibility in the interests of their stakeholders. This can improve employees’ satisfaction with the company, motivating them to work harder to raise productivity, thereby increasing the competitive advantage of the company’s products. It also helps to attract more customer resources, establish stable relationships with them and gain government trust. It can help to enlarge companies’ market share and ultimately increase corporate value to achieve sustainable development.

On the other hand, the use of ESG can also have a negative impact. Previous studies show that the benefits of using ESG are enjoyed by managers, but the risks and costs are paid by shareholders. Managers invest in ESG in order to improve their social status and personal reputation for their future career. Based on the reviewed theoretical materials and scientific research, the purpose of further work is to determine the effect of non-financial statements on the company’s financial performance and its position in the market. Most studies are limited to analysis of non-financial information disclosure impact on the companies’ financial performance. The most common is the analysis of such indicators as return on equity (ROE), return on assets (ROA), Q Tobin.

Let us consider in more detail how the authors of the articles determine the companies’ financial efficiency indicators.
to assess the impact of non-financial reporting on financial performance. They relied on these indicators to analyze companies from the oil and gas, chemical, and coal industries and came to the conclusion that the assessment of the environmental component of these companies is much higher than the same indicator of other organizations not related to fuel. In addition, it was concluded that there is a significant connection between the assessment of the organization’s environmental component and the return on equity.

Ong and other authors [13] of the article used return on assets (ROA), return on equity (ROE) and earnings per share (EPS) as corporate financial indicators. In another study of the authors [14], the methodology was based on the analysis of the impact of assessments separately for the environmental component (E), social (S), corporate (G) on ROA indicators. The study was based on data from 42 listed companies from the Chinese energy industry over 5 years (210 observations in total).

As a result, a positive correlation was obtained between the social assessment of the company and this indicator, as well as a negative relationship of the environmental assessment and the return on assets. This conclusion is quite interesting and, most likely, is associated with significant additional costs for solving environmental problems.

Another interesting study analyzing the possible relationship between the profitability of organizations and the disclosure of non-financial information was done by Mahmut Aydogmus Guzhan Gulay [15]. Based on the results of four models, the authors found a positive and significant connection between ESG indicators and the profitability of companies.

Investment preferences change regularly, following the international agenda, and now the most attractive organizations are those that comply with the international principles of ESG. The most obvious form of compliance is the issuance of green and social bonds to attract investment. Thus, according to the Royal Bank of Canada, 65% of respondents prefer green bonds, 50% choose social bonds. Therefore, in order to comply with the agenda, it is necessary to carry out similar activities in the agricultural sector. Successful practices are available in the Russian Federation. For example, this is the issue of green bonds of JSC "Russian Railways". Earlier, in 2021, the Dom.RF has issued the first "social" ICBS in Russia in accordance with the principles of ICMA social bonds (SBP). The will to use more tools such as green and social bonds shows the need for other companies in the market to follow this trend.

Fig. 1. Global ESG ETF assets from 2006 to February 2022 (in billion U.S. dollars)
According to Statista, the volume of assets under fund management increased by $373 billion from 2006 to 2022, slightly decreasing from 2021 to 2022 (Fig. 1.). In addition, the share of sustainable investments managed by managers increased from 27.9% to 35.9% from 2016 to 2020, which indicates that more and more companies are trying to meet the ESG agenda.

Currently, there are many standards that regulate the publication of non-financial statements, but there is no single regulatory document. In this regard, there is a problem of comparability of the reporting that different companies make because they compile their non-financial report according to different standards. The statistics of the conducted research on the applied standards in 2021 are given below (Fig. 2). It can be noted that the most commonly used standard is the Global Reporting Initiative.

A similar situation is also presented in Russia. In our study, we focused on Russian organizations that also apply the practice. According to the National Register of Corporate Non-financial Reports, the number of non-financial reports increased from 7 to 97 publications in the period from 2000 to 2021 (Fig. 3.).

As you can see, since 2014, the company's focus has shifted from the social report to the Sustainable Development report. In general, this interest can be associated with the creation of the Sustainable Development Goals (SDGs), which were agreed by the UN in 2015.
Russian companies actively publish and disclose non-financial information. The most advanced in this area are the companies from the energy sector (327 reports or 24% of the total for all time) and oil and gas industry. This is due to the fact that these industries actively influence the ecology of the country, and most companies in these industries are public. Shareholders want to know how these organizations neutralize the effect of their activities.

In addition to the energy sector, oil and gas industry has a large share (14% or 196 reports for the period from 2000 to 2021), as well as metallurgical and mining industries (14% or 192 reports). These companies disclose such information due to the similar factors as organizations from the energy sector do: they are public and make big damage to the environment.

Generally, the most popular form of reporting is the sustainable development report (52%) and the integrated reporting (41%). At the same time, an interesting point is that in 2000 only 7 reports were published: 3 environmental reports (PJSC Tatneft, LLC Neman Pulp and Paper Mill (CJSC SZLK), JSC Ryazan GRES) and 4 social reports (JSC Lenenergo, PJSC MMK, JSC MHC EuroChem, Union of Russian Brewers).

3 Conclusion

It can be concluded that there are significant risks for agricultural enterprises in not reflecting ESG principles in their non-financial reporting. The society can evaluate the efforts of companies to follow these principles only through non-financial reporting. The conducted research showed that despite the fact that some large agricultural enterprises are actively engaged in financial and investment activities and their securities are listed on the stock exchange (AVANGARD-AGRO JSC, AgroElita Association LLC, etc.), their non-financial reporting does not comply with the currently existing standards based on ESG principles. At the same time, the Russian Federation has advanced practices for the formation of non-financial reporting, which should be used by agricultural enterprises to reduce the risks of activity in the new economic conditions.

References


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