



**UNIVERSITY  
OF TURKU**

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Economics

# **How does ESG reporting affect investment decisions by financial institutions?**

A case study on the impacts of CSRD and SFDR on the food industry

Accounting and Finance

Master's thesis

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Sustainability reporting is undergoing a fundamental change with new regulatory requirements implemented by the European Union. The Corporate Sustainability Reporting Directive (CSRD) which came into force in 2024, will significantly influence the sustainability reporting processes of both companies and financial institutions. This Directive introduces new reporting obligations that will progressively apply to companies of varying sizes over the coming years, putting a strain on the reporting obligations of smaller firms. Alongside the Sustainable Finance Disclosure Regulation (SFDR), the CSRD is essential in driving the financing of the green transition.

The thesis was conducted as a case study for the Finnish food and dairy company Valio where the main research question seeks to analyse the ESG factors affecting investment decisions by financial institutions. The aim was approached by examining the relevant sustainability risks and aspects in the food industry from a financier's perspective. The shift from voluntary to mandatory sustainability reporting reflects how sustainability reporting is increasingly integrated with financial analysis. Prior research found evidence on the lack of transparency, reliability and comparability in the current sustainability reporting landscape. Investors have criticized the high degree of subjectivity in sustainability reports, hindering the ability to make informed decisions. The theoretical framework of this study is based on previously established sustainability directives and their demonstrated impacts within the food industry.

The methodology used in this research is a qualitative assessment of six semi-structured interviews. For the purpose of this study, the data was collected by anonymously interviewing ESG-professionals working in the financial sector from different financial institutions. Consequently, recordings were transcribed using Microsoft Teams and the UTU Transcribe Service. The processed data was then divided into three main themes based on the research questions and interview answers: sustainable finance and auditing, sustainability in the agri-food sector and ESG-based financing.

The study yielded several findings. First, the supply chains of food companies is critical to food security and their sustainability performance. Second, financial institutions tend to rely on climate-related indicators when establishing financing terms because they are currently the most reliable. Third, behavioural changes in consumer preferences pose risks to the food industry that may affect the future cash flows of food companies. Finally, financial institutions continue to value the risk/return ratio of green projects. Companies must prove that sustainability targets are realistically achievable to receive financing.

**Key words:** Sustainability reporting, CSRD, SFDR, food industry, financing

Pro gradu -tutkielma

**Oppiaine:** Laskentatoimi ja rahoitus

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**Otsikko:** Miten ESG-raportointi vaikuttaa rahoituslaitosten investointipäätöksiin? – Tapaustutkimus CSRD:n ja SFDR:n vaikutuksista elintarviketeollisuuteen

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Vastuullisuusraportointi on murroksessa, kun Euroopan Unioni on ottanut käyttöön uusia sääntelyvaatimuksia. Vuonna 2024 voimaan tullut yritysten kestävän kehityksen raportointia koskeva direktiivi (CSRD) vaikuttaa merkittävästi sekä yritysten että rahoituslaitosten kestävän kehityksen raportointiprosesseihin. Direktiivillä otetaan käyttöön uusia raportointivelvoitteita, joita sovelletaan asteittain erikokoisiin yrityksiin tulevina vuosina, mikä rasittaa pienempien yritysten raportointivelvoitteita. Kestävän rahoituksen julkistamista koskevan asetuksen (SFDR) ohella CSRD on olennainen tekijä vihreän siirtymävaiheen rahoituksen edistämässä.

Tutkielma on toteutettu tapaustutkimuksena suomalaiselle elintarvike- ja meijerialan yritykselle Valiolle, jonka tutkimuskysymyksenä on selvittää rahoituslaitosten sijoituspäätöksiin vaikuttavia ESG-tekijöitä. Tavoitetta lähestyttiin tarkastelemalla elintarviketeollisuuden liittyviä kestävyysriskejä ja -näkökohtia rahoittajan näkökulmasta. Siirtyminen vapaaehtoisesta kestävyysraportoinnista pakolliseen kestävyysraportointiin on osoitus siitä, että kestävyysraportointi on yhä enemmän integroitunut taloudelliseen analyysiin. Aikaisemmissa tutkimuksissa on saatu viitteitä avoimuuden, luotettavuuden ja vertailukelpoisuuden puutteesta nykyisessä kestävän kehityksen raportoinnissa. Sijoittajat ovat kritisoineet kestävyysraporttien korkeaa subjektiivisuutta, joka hankaloittaa tietoon perustuvien päätösten tekemistä. Tutkimuksen teoreettinen viitekehys pohjautuu aikaisemmin luotuihin kestävän kehityksen direktiiveihin ja niiden havaittuihin vaikutuksiin elintarvikealalla.

Tutkimuksen metodologiassa on käytetty laadullista tutkimusmenetelmää, joka koostuu kuudesta puolistrukturoidusta haastattelusta. Tutkimuksen aineisto on kerätty haastattelemalla nimettömästi eri rahoituslaitosten ESG-ammattilaisia, jotka työskentelevät rahoitusalalla. Tämän jälkeen nauhoitukset litteroitiin Microsoft Teamsin ja UTU Transcribe -palvelun avulla. Käsitelty aineisto on jaettu kolmeen pääteemaan tutkimuskysymysten ja haastatteluvastausten perusteella: kestävä rahoitus ja tilintarkastus, kestävä kehitys maatalous- ja elintarvikealalla ja ESG-perusteinen rahoitus.

Tutkimuksesta saatiin useita havaintoja. Ensinnäkin elintarvikeyritysten toimitusketjut ovat kriittisiä elintarviketurvan ja niiden kestävän kehityksen suorituskyvyn kannalta. Toiseksi rahoituslaitokset sitovat rahoitusehtonsa yleensä ilmastoon liittyviin indikaattoreihin, koska niitä pidetään tällä hetkellä luotettavimpina. Kolmanneksi kuluttajakäyttäytymisen muutokset aiheuttavat elintarviketeollisuudelle riskejä, jotka voivat vaikuttaa elintarvikeyritysten tuleviin kassavirtoihin. Lisäksi rahoituslaitokset arvostavat yhä ympäristöystävällisten hankkeiden riski-tuottosuhdetta. Yritysten on osoitettava, että niiden kestävyystavoitteet ovat realistisesti saavutettavissa saadakseen rahoitusta.

**Avainsanat:** Vastuullisuusraportointi, CSRD, SFDR, elintarviketeollisuus, rahoitus

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## List of abbreviations

CSR	Corporate Social Responsibility
CSRD	Corporate Sustainability Reporting Directive
EBA	European Banking Authority
EC	European Commission
EFRAG	European Financial Reporting Advisory
EIOPA	European Insurance and Occupational Pensions Authority
EMAS	Eco-Management Audit Scheme
ESMA	European Securities and Markets Authority
ESRS	European Sustainability Reporting Standards
EU GBS	EU Green Bond Standards
GBP	Green Bond Principles
GRI	Global Reporting Initiative
HLEG	High-Level Expert Group on Sustainable Finance
ICMA	International Capital Market Association
IFRS	International Financial Reporting Standards
IIRC	International Integrated Reporting Framework
ISSB	International Sustainability Standards
MiFID II	Markets in Financial Instruments Directive II
MiFIR II	Markets in Financial Instruments Regulation II
NFRD	Non-Financial Reporting Directive
SASB	Sustainability Accounting Standards Board
SBG	Sustainability Bond Guidelines
SBP	Social Bond Principles
SFDR	Sustainable Finance Disclosure Regulation
TCFD	Task Force on Climate-related Financial Disclosures
UN GPRF	UN Guiding Principles Reporting Framework

# 1 INTRODUCTION

## 1.1 Background and motivation of the thesis

Sustainability reporting is in the midst of structural changes applied by the European Commission (EC) that is changing how companies with business operations in the European Union (EU) report on sustainability matters. Corporate sustainability reporting has existed for far less than traditional financial reporting although constant active measures taken by governments or other legal bodies during the recent years has solidified its place as part of the accountability obligations for companies. The Sustainable Development Goals introduced (SDGs) in 2015 by the United Nations (UN) played a pivotal role serving as a catalyst for companies to integrate these goals into their operations and strategies (Costa et al., 2022).

Non-financial reporting is no longer carried out just as a voluntary practice to showcase a company's commitment to sustainable and responsible business practices in EU firms. Increasing pressure from a variety of stakeholders including non-governmental organizations (NGOs), investors and consumers has forced new European legislations to put into place in order to ensure that companies take their non-financial reporting seriously and remain accountable for their actions. This shift from voluntary practice to mandatory reporting is driven by the growing recognition of the integral role that businesses play in addressing environmental, social, and governance challenges on a global scale. (De Silva Lokuwaduge & De Silva, 2022; Rezaee et al., 2023)

The European Commission has taken steps to put forward more stringent regulations that measure the sustainable performance of companies that operate under the EU's jurisdiction. However, previously implemented sustainability frameworks like the Directive 2014/95/EU have received a substantial amount of criticism from stakeholders who contended that the sustainability reports fell short of providing comprehensive details on significant sustainability matters. This includes climate-related information particularly greenhouse gas emissions, and the effects on biodiversity. Other shortcomings were identified in the limited comparability and reliability of the data which has caused serious problems when trying to assess the impacts of a company. Christensen et al. (2021) have also pointed out that sustainability information is typically industry-specific and harder to quantify. Moreover, the European Commission has discovered a

need for a more robust reporting framework that includes a broader range of companies that have not been obliged to report such information before in the NFRD (European Commission, 2023a; Aureli et al., 2020)

Ever since Corporate Social Responsibility (CSR) has increased in demand, there has been a lack of harmonised reporting requirements and ways to communicate with external stakeholders. Investors have claimed that these reports lack credibility and their high degree of subjectivity hinders the ability to make informed financial decisions (Arvidsson & Dumay, 2022; García-Sánchez, 2020). There is a large body of scientific literature that questions the usefulness of sustainability disclosures, stating that companies engage in such activities to protect their own interests and that sustainability commitments often go unfulfilled (Adams, 2004; Boiral, 2013; Milne & Gray, 2013; Patten, 2012).

The European Commission aims to fulfil the information gap between stakeholders and companies to decrease the scepticism around the current sustainability reports which often lead to higher costs in the capital markets (European Commission, 2023a; Fink, 2020). The timeline for the new changes is short, making this study significant and relevant for an increasing number of companies under EU jurisdiction. These new rules will have to be enforced for the first time in the 2024 fiscal year and the reports are expected to be released in 2025 according to the EC. The European Parliament has estimated that around 50 000 companies will fall under the scope of the new regulations compared to the previous 11 700 required to report under the Non-Financial Reporting Directive (NFRD). This means that the upcoming changes will apply to small and medium-sized enterprises as well which will be subject to simplified reporting standards. (European Parliament, 2022)

Therefore, the aim of the study is to address the new changes in the European sustainability landscape by analysing the impact of the new Corporate Sustainability Reporting Directive (CSRD) and how it affects financial institutions' disclosure strategies when investing in companies under the scope of the CSRD. Creditors in the agribusiness industry must be aware of these changes as they provide more detailed information on the non-financial activities of agrifood businesses. This will allow creditors to reassess the risk profile of companies in the context of these new obligations.

The thesis will be carried out as an assignment for a company in the food industry, Valio Oy, which will not only help them prepare for the new EU regulations on sustainability

reporting but also give a deeper understanding on what are the key aspects for financial institutions in regard of food industry investments and financing operations. The evolving dynamic between sustainability reporting and corporate financing has become increasingly more relevant, ever since financiers have begun to include ESG (Environmental, Social and Governance) factors into their decision-making (European Commission, 2021). The thesis will also provide guidance for the company, and the industry in general, to understand on a tangible level about interests and preferences of financiers to food safety organisations. The thesis also seeks to distinguish between voluntary sustainability reporting, which supports agenda development and communication with stakeholders, and mandatory ESG reporting enforced by EU regulation. The agri-food sector also acts as a strategic tool for food security and environmental conservation in Europe (European Commission, 2019).

On a personal note, I am interested to learn more about the future guidelines and evolution of sustainability reporting. Sustainability has existed for several years, but it has developed into various forms over the years and regulations have struggled to keep up with the continuous global change happening in the financing markets. The importance of ESG today extends beyond just the normative and regulatory framework to a more responsible way of investing and overall corporate governance. It remains with significant potential to unlock new ways of value creation which is why it is an important tool for any company to focus on for growth. International organisations are adapting to the changes in the European regulatory environment which will also increase the demand for sustainability related skills and knowledge. Sustainability expertise will most likely become a critical asset for businesses if they want to ensure sustainable growth in a future where sustainable solutions will thrive.

## **1.2 Research question and objectives**

The main research objective of the case study is to find how ESG reporting affects investment decisions made by financial institutions, especially in the food industry. The thesis will look for a solution through the lenses of CSRD and SFDR, two recently announced and updated directives changing the way sustainability reporting will be produced. Sustainability is considered an umbrella term which spans many different business areas, which is why this thesis focuses on the regulative frameworks of the Corporate Sustainability Reporting Directive (CSRD) and Sustainable Finance

Disclosure Regulation (SFDR). The main difference between the two is the target groups for which they are intended to influence. The CSRD requires EU companies to publish mandatory sustainability metrics and the impact of their activities on society and the environment. On the other hand, the SFDR is targeted at financial market participants (FMPs) and financial advisors i.e. banks, investment firms, insurance companies, venture capital funds, etc. that must use the SFDR standards when disclosing sustainability-related information. Both of these disclosure requirements are part of the broader EU sustainable finance framework which is intended to integrate sustainability factors across all levels of the economy. (European Commission, 2023a.) In order to examine the two frameworks in the same context, a case study using qualitative research methods is implemented. Qualitative techniques allow the researcher to identify the underlying relationship between the two phenomena and collect data to support the research's objectives. The interview method was considered to be the most appropriate for identifying the expectations and requirements of the case company. (Gillham, 2000.)

The research question specifically seeks to explore sustainability issues in the food sector from the perspective of financiers. More detailed sub-questions will try to find answers for different aspects of the reports and financing matters. The sub-questions may refer to the risks that financial institutions consider in sustainability-related reports or aspects that are particularly important to financial institutions in relation to the food industry and Valio.

The research sub-questions are as follows:

1. What kind of sustainability-related risks financial institutions consider the most relevant in the food industry?
2. What aspects are particularly important to financial institutions in the food industry and Valio?

The first research sub-question attempts to identify which sustainability risks are most important to financial institutions when evaluating investments in the food business. This might include industry-specific risk factors such as procurement, waste management, or the carbon impact of food manufacturing and transportation. The second sub-question examines the attractiveness of food industry actors, particularly Valio, to financial institutions. The aim of the sub-question is to discover specific components that financial

institutions consider critical when investing in the food business. Finding a solution to these issues will be helpful for companies finding themselves in similar situations to Valio. The research questions and sub-questions will also serve as grounds for future business opportunities relating to ESG reporting between companies operating in the EU and outside of it.

### **1.3 Contributions**

This study takes a detailed look at the CSRD implemented by the European Commission and focuses on its implications mainly on the financial industry. First, it contributes to the theoretical literature on sustainability by addressing the unexplored implications of this new regulation for financial institutions. The study deep-dives into the domain of mandatory sustainability reporting, a relatively under-researched area, by investigating whether such mandatory disclosures reduce information asymmetries, improve comparability, and generate cost benefits for both firms and stakeholders (Christensen et al., 2021). The evidence confirms previous research on mandatory sustainability disclosures and suggests that they can shift business practices and achieve positive social outcomes (Chen et al., 2018).

Secondly, there are managerial implications for Valio and other Finnish food companies in the scope of CSRD that are preparing for the regulation changes in advance. The Corporate Sustainability Reporting Directive should not be seen merely as a regulatory mandate but as a strategic business opportunity, especially for larger European companies. These companies can ensure a competitive advantage by successfully navigating the necessary adjustments required by the CSRD. This will require preparatory work to identify gaps in their sustainability reporting frameworks that need to be addressed in order to comply with the Directive. Key priorities include reporting on intangible assets, ensuring that the company's business model and strategies are aligned with the EU's climate neutrality objectives, and disclosing information related to the company's value chain. As illustrated by the empirical findings, sustainability reporting will increase, which is likely to stimulate new sustainability initiatives. Financial materiality analyses are expected to increase the importance of sustainability reporting and bring it more closely in line with financial reporting through the CSRD and the EU Taxonomy. Furthermore, changes to assurance requirements will transform the way

companies operate by improving processes to accommodate machine-readable formats and to comply with limited audit assurance.

Thirdly, the shift towards more transparent sustainability reporting at a company level improves the quality of sustainability disclosures of investment products driven by the SFDR. The empirical findings have resulted in practical contributions to financial institutions. Their internal investment processes will undergo a transformation in the due diligence of target companies, to which this study brings insights. The results provide a holistic understanding of the risk profile in the food industry and what its high-impact aspects are compared to other industries. This is particularly important when assessing the long-term viability and resilience of companies in the food sector, ensuring that investments align with both financial and ESG performance criteria.

To conclude, this thesis confirms the need for regulatory change in the EU sustainability landscape as highlighted in previous studies. It serves as a useful tool for food companies, financial institutions and investors looking to prepare for the upcoming EU reporting requirements and which aspects of reports are the most important for the food industry. The results and implications of this study may also be applicable to other companies covered by the CSRD and to financial institutions falling under the SFDR.

#### **1.4 Structure**

The study is divided into seven different sections, which are further split into smaller subsections that open up the contents of the sections in more detail. The first section serves as an introduction to the topic setting the foundation for the rest of the study that involves a deeper understanding of the topic. The section formulates the research questions and related sub-questions that will be analysed throughout the study. It sets a clear objective for the research, which the study consistently seeks to address. The second section provides a fundamental review of the sustainability framework especially in Europe and a terminology analysis of the most important concepts of sustainability reporting touching this study. The aim of the terminology analysis is to facilitate the understanding of sustainability legislation and other various abbreviations that might be difficult to conceptualize for the reader.

The third section consists of a literature review of the current scientific literature available which aims to support the empirical research of the study. It discusses the underlying

theories involving sustainability reporting and the dynamic relations between stakeholders, especially financial institutions and companies. This section will dive deeper into the meanings of ESG metrics for financial institutions, how the new EU directives affect investment decisions in the food industry and what kind of risks are involved in it. Additionally, it will also break down existing scientific findings on the impact of sustainability reporting in financing decisions. The fourth section is divided into three parts covering the data collected for the empirical research, the method used for the qualitative analysis of the study and ethical considerations related to the research.

Sections five and six will consist of presenting the results of the study followed by a deeper analysis of the interviews, which will aim to combine the findings from the theoretical part with the empirical research. In the discussion section, the thesis will also offer managerial implications, an evaluation of the study which examines the integrity and authenticity of the research process. Additionally, limitations and further research suggestions are provided. The thesis will answer the research questions and sub-questions accordingly and make final statements on the objectives of this research in the last section. In section seven, the summary will draw together the conclusions of the study and summarise the research process in a clear and concise way, with the aim of giving an overall picture of the study and its purpose.

## **2 ESG LEGISLATION IN EU**

### **2.1 European Commission's sustainability landscape**

#### **2.1.1 Review of the European Green Deal and NFRD**

The European Green Deal is a comprehensive growth strategy that aims to make the European Union (EU) climate neutral by 2050 while ensuring a fair and prosperous transition for all stakeholders. Climate neutrality refers here to producing zero net greenhouse emissions whilst decoupling economic growth from resource use. It covers various policy areas, such as energy, transport, industry, agriculture, biodiversity and finance, and proposes concrete actions to achieve the EU's climate goals. The European Union has stated its ambitions to become the first climate neutral continent, and actively engaging in developing clearer and better policies is evidence for it. (European Commission, 2021.) The strategic plan represents a broader legally binding framework which is then translated by the Action Plan proposed first in 2018 and adopted in 2020 by the EC. The Action Plan introduces a set of concrete legislative proposals to address the challenges and objectives of the European Green Deal. It is a first step towards the roadmap set out in the European Green Deal and towards a common definition of what is and is not sustainable. (European Commission, 2020)

The European Commission, in cooperation with the High-level expert group on sustainable finance (HLEG) it has set up, has approved a set of initiatives implementing several key actions that can be categorized into three sections: Redirecting capital flows towards a more sustainable economy, mainstreaming sustainability into risk management and encouraging transparency and longevity. The first category entails the cornerstone of the EU's sustainable finance framework, which is the EU Taxonomy Regulation. It creates the foundation by laying four fundamental criteria that economic activities must fulfil in order to be considered environmentally friendly. Addressing the lack of criteria is crucial for achieving the needed environmental and social investment targets. Investors do not have a sufficient understanding of what constitutes a sustainable investment which prevents the EU from meeting its climate and energy targets because not enough capital is being redirected towards transport, energy and resource management infrastructures. According to the PRIMES model by the EC, the European Union must increase its sustainability efforts by almost 180 billion euros. That gap can only be achieved if the

current problems of inequality and inclusion are addressed. (European Commission, 2018)

The European Union sees this challenge as an opportunity to play a leading role in the coordination of international efforts in the field of sustainability. Its objective is to eventually create a unified and transparent financial system that promotes the development of sustainable projects. It also understands that it cannot change the course of action alone because biodiversity losses, social and governance issues are not limited to European borders. Hence, the EU is actively creating global partnerships and alliances which will encourage organisations to commit to the policies and directives implemented by the EC. (European Commission, 2019)

The European Green Deal encompasses a multitude of proposals from the EC that have all been adopted. This legislation package has been named “Fit for 55” which stands for the 55% of greenhouse gas emissions that need to be reduced by 2030. The last two pillars of the package were adopted in October of 2023. The full adoption of the legislation package is a sign to the European Commission’s partners that it can deliver and even exceed its promises. (European Commission, 2023c.) In terms of investor support, a new EU Green Bond Standard was adopted in October of last year which is part of the first initiative approved by HLEG. It became a major step towards providing sustainable instruments for financing green technologies and the regulation will help prevent green bonds from being greenwashed due to its uniform requirements for issuers of bonds. (European Council, 2023.)

In 2018, the Directive 2014/95/EU (also known as NFRD) came into effect after four years of adoption and it marked a definitive course of action for the European sustainability landscape. The NFRD was an update of the previous Accounting Directive and has broadly the same objectives as the most recent Directive 2022/2464/EU (the so-called Corporate Social Reporting Directive), which recognizes the key role of the private sector in financing the green transition by increasing transparency and accountability of companies. It required companies to take responsibility on matters such as environmental, social and employee matters, human rights, anti-corruption and bribery. These issues were the minimum reporting obligations although exceeding these requirements would ultimately benefit trade unions and worker’s representatives who were more informed and therefore were able to engage in social dialogue. Nevertheless, the NFRD had many

shortcomings, and its policies were not sufficiently rigorous. (European Parliament, 2021; Krasodomska et al., 2023.) In the next section, we will get more into these issues.

### 2.1.2 Towards Corporate Sustainability Reporting Directive (CSRD)

The implementation of the Corporate Sustainability Reporting Directive (CSRD) has presented several complexities, particularly for companies with limited prior engagement in sustainability reporting. These organizations now face the challenge of acquiring and reporting additional credible data to comply with the stringent requirements of the Directive. Companies with existing experience in voluntary sustainability reporting and reporting on the Sustainable Development Goals are anticipated to lead the way in adapting to this evolving regulatory landscape. (Krasodomska et al., 2023)

The need for changes in the regulatory landscape of the EU will have an effect on multiple established directives by the EC such as the Transparency Directive 2004/109/EC, the Audit Directive 2006/43/EC and the Accounting Directive 2013/34/EU. Additionally, the CSRD will bring changes to Regulation 537/2014 regarding the requirements of statutory audit of public-interest entities in the EU as it will mandate companies to have their sustainability reports assured initially to a limited assurance engagement and afterward to a reasonable assurance engagement no later than by 2028. The aim of these requirements is to enhance the credibility of these reports since the statutory audit will have to be conducted by an accredited independent auditor. Thus, supplementary assurance for the sustainability reports is needed which will also aim to open up the current audit market from the hands of a small number of operators. (European Commission, 2023a; Krasodomska et al., 2023)

The principal goal behind this new framework is to provide stakeholders and investors with complete and trustworthy sustainability data, allowing them to assess a company's commitment to sustainability principles. As a result, organizations subject to the Directive's obligations must properly understand its provisions and examine the effects on their legitimacy and reporting procedures, which have important practical and operational consequences (Glaveli et al., 2023). Companies that can utilize the CSRD to analyse their organization from an ESG viewpoint will have a valuable tool for gaining insights into business risks and possibilities. According to a research paper from KPMG, the Directive can help to improve the implementation of a company's ESG strategy and provide clarity on how these targets are measured. Only time will tell if the Directive will

accomplish all the objectives for which it has been created and bring the needed transparency in the regulatory environment (KPMG 2022b).

The European Financial Reporting Advisory (EFRAG) has developed a set of standards that companies under the new Directive must follow. The European Sustainability Reporting Standards (ESRS) are created in accordance with other EU policies and international sustainability frameworks making it easier for organization to embrace the green transition. The standards have been developed together with interest organizations, national bodies and representatives of analysts and investors. To address all the impacts, risks and opportunities in relation to sustainability matters, the ESRS Standards are divided into three categories:

1. Cross-cutting standards
2. Topical ESG standards
3. Sector-specific standards

The first category establishes the general requirements and explains the fundamental concepts for preparing and presenting sustainability-related information. The cross-cutting standards are divided into ESRS1 and ESRS2 both being mandatory. The ESRS 1 outlines reporting areas that are necessary to understand the impacts, risks and opportunities of the company with regard to ESG aspects. This includes areas such as qualitative characteristics, due diligence procedures, value chain information, stakeholder identification and the definition of the new double materiality assessment to name a few. The purpose of the double materiality principle is to identify both the financial materiality and impact materiality of a company. The former requirements stated in the NFRD mandated companies to identify sustainability-related impacts on the company or in other words, the financial materiality. The double materiality extends this concept to also account for the impacts of a company on the environment and other aspects of ESG which is called the impact materiality. Combining the results of both assessments produces a comprehensive and more complex analysis that extends beyond the organisation's internal operations. The European Commission's reasoning behind this new accounting concept is the lack of useful data from the previous one-dimensional model. European institutions have voiced their concerns over adopting disclosure requirements to fill the data gap caused by it. Critics on the other hand have claimed that the double materiality assessment

can result in an overload of information and increased information costs, particularly for smaller entities. The second part of the first category is the ESRS2 which explains the so-called “cross-cutting” areas that also apply to the topical standards below. It presents four pillars that must be provided in the report regardless of the sustainability relevance. These are impacts, risks and opportunity management, governance, strategy and metrics and targets.

Beyond the foundational prerequisites, the ESRS offers ten optional topical standards in within the second category. These topical ESG standards form specialized frameworks that are tailored for specific sectors to evaluate and report their sustainability performance. While they are not mandatory, these topical standards play a key role in enabling organisations to comprehensively disclose their sustainability practices and impacts in specific ESG areas. The third category consists of sector-specific standards that will affect all firms in a specific sector. This category recognizes the diverse nature of industries and addresses the impacts, risks and opportunities that might be adequately covered by the previous categories. The aim of sector-specific standards is to achieve a high degree of comparability and target relevant sustainability areas in a sector.

In 2021, KPMG conducted a study that examined the readiness of Dutch companies to comply with CSRD reporting standards. It assessed key areas such as double materiality reporting, target setting, progress disclosure, and assurance readiness. The report highlighted that despite recognizing the importance of ESG reporting, many companies struggled to align their business models, operations, and strategies with sustainability transitions, particularly in addressing environmental, social, and governance issues. Environmental disclosures received considerable attention, likely driven by stakeholder pressure on climate-related concerns, while governance disclosures were relatively more developed. However, social disclosures tended to focus on the reporting company itself, with limited coverage of social aspects within the supply chain. Even though the study was limited to Dutch companies, it provides key insights into companies’ progress to sustainability reporting. The CSRD reporting standards have also been further improved in more detail since the report was published, so companies are now better equipped to prepare for the CSRD disclosure requirements. (KPMG, 2021)

### 2.1.3 Adjusting the Sustainable Finance Regulation Disclosure (SFDR)

Shortly after the adoption of the first Action Plan on financing sustainable growth, the EC introduced the Sustainable Finance Regulation Disclosure (SFDR) with the objective of bringing transparency to the market for investment products that claim to be sustainable. The SFDR provides a classification of investment products that facilitates their comparability and allows investors to better understand the implications of their investment decisions. The detailed disclosure requirements, which have been applied since March 2021, are designed to channel private capital into more sustainable businesses and activities in order to support the objectives of the European Green Deal. (Eurosif, 2022; European Commission, 2019)

The SFDR is a more rigorous regulation that stands out from the recommendations from rating agencies and other market participants and sends a signal to the world of the EU's proactive attitude that could serve as a guide to other major economies in North America and Asia, for example. The SFDR reporting framework applies to every asset manager and other financial market participants who market funds or products within the EU making it also a relevant part of this study. To give a brief illustration of the SFDR classification, the requirements can be divided into product-level and entity level disclosures:

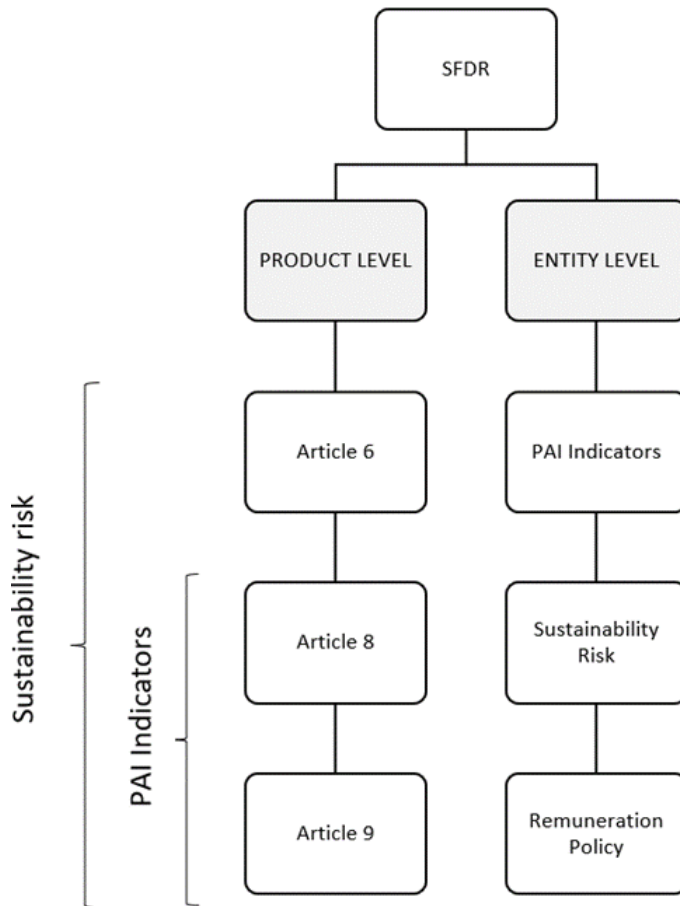


Figure 1 SFDR reporting framework classification (modified from ESGTree.com, 2023)

At the product or fund level, the SFDR classifies them as either an article 6, 8 or 9 product. In principle, Article 6 requires asset managers to disclose how sustainability risks are considered in their funds, regardless of whether the funds are being promoted as ESG-friendly or not. However, investments that are promoted as ESG-friendly must be classified under either Article 8 or Article 9, depending on which specific classification criteria their financial offer meets. Article 9 funds have higher requirements because their main objective is sustainable investment. Whereas article 8 products promote “environmental or social characteristics” among other good governance practices. (European Commission, 2021)

At the entity level, financial market participants, along with financial advisors, need to demonstrate how they integrate sustainability risks that could impact both their investments and broader societal well-being. This also extends to revealing whether they take into account Principal Adverse Impacts (PAIs) and how their remuneration policies reflect their consideration of these sustainability risks. (European Commission, 2021)

The SFDR follows a disclosure-based framework for classifying these sustainability requirements, which has been criticized for its broad scope. Although the categories are intentionally broad to cover a diverse variety of products to promote openness, using a framework intended for transparency and disclosure to classify products might pose major concerns. According to the European Sustainable Investment Forum (Eurosif) flexible thresholds for triggering Articles 8 and 9 have resulted in products being classified under both sections, and in some cases reclassified to include ESG factors that do not have a material impact on the investment process. (Eurosif, 2022.) Other institutions, such as Finance Finland or the AMF, have criticized the SFDR for the lack of standardisation in financial products and conceptual discrepancies especially in PAI disclosures (Finance Finland, 2023; AMF, 2022).

The European Commission has already taken steps to review the structure of the regulation, having gained practical experience of its impact. In September 2023, it launched two consultations to gather views on the effectiveness and consistency of the current framework, and to consider possible changes to the disclosure mandates. The consultations could add clarity to the article classifications and requirements which, in turn, could boost investor confidence. As such, the consultations could accelerate private investment in sustainable projects, which could lead to an increase in the volume of assets under management (AUM) and demand for green funds. (European Commission, 2023b)

In recent years, governmental measures have significantly improved access to credit for agricultural companies. Together with the evolving regulatory landscape and increased ESG investments, they can ease the financial burden on agricultural businesses which not only strengthens their social contribution but also supports businesses located in less advantaged regions or cooperatives such as Valio. (Bertinetti, 2023; Iotti, 2023.) The shift from traditional relationship lending towards a more market-oriented approach can already be observed in Italy's financial landscape (Bertinetti, 2023). The agri-food sector, characterised by its high exposure to ESG risks and the capital intensity of its production cycles, plays a key role in advancing the circular economy (Iotti, 2023). We are entering a new phase where companies that fail to disclose their sustainability actions and projects risk being excluded from capital and financial markets. Over time, this can result in being abandoned from the market altogether (Bertinetti, 2023; Briamonte et al., 2023).

## 2.2 A terminology analysis of ESG reporting

The growing number of sustainability and ESG reporting criteria, guidelines, and standards demonstrates the significant degree of interest in this subject. Subsequently, the development of such measures has posed challenges, particularly for foreign firms that must deal with legal, regulatory, and stakeholder demands in different jurisdictions. Companies, investor groups, and other stakeholders keep voicing concerns about ambiguity and fragmentation, as well as a lack of comparability and reliability of the reported information. The recent changes in the European institutional framework of CSR are leading to the adoption of clearer voluntary and intentional corporate actions. Matten and Moon (2008) and Hiss (2009) theorise that the emergence of explicit CSR in Europe is a consequence of the developments in the political, economic, educational and cultural institutional systems. (Hiss, 2009; Matten & Moon, 2008)

The European Commission has advised caution when using the term “non-financial” in the context of sustainability reporting as it is somewhat misleading because it conveys a lack of financial importance in the information being described. Yet, an emerging consensus acknowledges that this type of information does indeed carry financial significance and numerous entities and initiatives have adopted the use of the term “sustainability information”. (European Commission, 2023a.) The term has also been considered synonymous with “ESG reporting” which is mostly used by companies referring to their interactions with specific aspects of sustainability. To clarify the terminology around sustainability and minimise any confusion around its vocabulary, this section will contain a brief terminology analysis of the regulatory and voluntary framework of sustainability. Especially for a lot of readers who are new to the space or do not regularly follow the development of worldwide sustainability effort it can be tricky to get a grasp of the larger picture. Since there are countless of international and national institutions, advisory bodies and NGOs that are involved in developing sustainability reporting systems, the framework of this study is limited only to the most relevant ones in the context of this study. The objective is to provide an understanding of the most relevant and up-to-date abbreviations of sustainability reporting without necessarily describing their purpose, history or scope.

NGOs around the world are pushing for stricter regulation of corporations to increase their awareness of their direct and indirect impacts of their operations on society.

Standard-setting bodies such as the EFRAG, the International Organization for Standardization (ISO) or the International Sustainability Standards Board (ISSB) among others, provide their own frameworks and guidance for companies to try to achieve the objectives set by political institutions, such as the United Nations (UN). While NGOs do not have legislative power over the jurisdictions of other countries, their governments usually follow on by adopting their guidelines and implementing them in their laws.

The purpose of this terminology analysis is to establish a clearer framework for the sustainability vocabulary that may be confusing to a number of investors, institutions, companies and even professionals working in the field. Each relevant abbreviation related to this study will be briefly explained to facilitate the reader's understanding of specific terms as he or she proceeds forward with the paper.

Table 1 Sustainability reporting landscape

<b>Target area</b>	<b>European Union</b>		<b>Global</b>	
<b>Target group</b>	Companies	Financial capital providers	Companies	Financial capital providers
<b>Components</b>				
<b>Regulations and Directives</b>	NFRD, CSRD, EMAS, CSDDD	SFDR, MiFIR II, MiFID II		
<b>Supervisory and Regulatory Authorities</b>	ESA (EBA+ ESMA+EIOPA), EFRAG, HLEG		ISSB, SASB, IIRC, CDP	ICMA
<b>Reporting Standards and Frameworks</b>	ESRS	EU GBS	GRI, IFRS S1+S2, UNGP RF, TCFD	TCFD, SASB, SBG (GBP+SBP)

Table 1 provides a classification of the intricate and complex abbreviations of the sustainability reporting landscape highlighting the distinct but interconnected roles of various regulations, supervisory bodies, and reporting standards across two regions.

Table 1 shows how the sustainability reporting landscape is divided into three main components, each classifying its own entities. The terms are further divided into two

target groups, companies and financial capital providers, and two target areas, into the European Union and globally. Since the terminology for sustainability is much broader, we will only focus on vocabulary that is relevant to this study. The framework does not address terms related to financial reporting, although it is challenging to draw a line between this and sustainability reporting. Future developments in reporting standards suggest that these two areas will become more coherent and integrated as part of a broader business performance reporting framework (SASB, 2023).

### 2.2.1 European Union

In Europe, sustainability reporting is governed by the European Commission which proposes and enforces EU law. The European Union could be considered at the forefront of sustainability legislation which has actively implemented a multitude of regulatory requirements and voluntary initiatives which are designed for companies and financial institutions to disclose their ESG practices in a transparent and comparable manner. One of the foundational elements of in this landscape is the Corporate Sustainability Reporting Directive (CSRD) which is a continuation of the Non-Financial Reporting Directive (NFRD). Another important initiative is the Eco-Management and Audit Scheme (EMAS) which is a voluntary environmental management tool to improve material and resource efficiency. Although it is not mandatory, the EMAS certification is based on the dedicated EMAS Regulation (European Commission, 2009). Completing this section is the Corporate Due Diligence Directive (CSDDD) which was recently approved by the European Parliament in April (European Parliament, 2024).

Financial capital providers require their own regulatory framework in order to ensure transparent disclosure of their investment products. Here, the Sustainable Finance Disclosure Regulation (SFDR) plays a major role in imposing specific categorization for these products mentioned in section 2.1.3. Additionally, the Markets in Financial Instruments Regulation II (MiFIR II) and the Markets in Financial Instruments Directive II (MiFID II) aim to provide investor protection and consolidated market data especially when performing shorter-term investing also known as “trading”.

There are a lot of supervisory and regulatory authorities that have been established or formed by the EC. The framework only contains some of the most important ones related to sustainability reporting. The first one on the list, European Supervisory Authorities (ESA), is actually a term used to describe the three agencies: the European Banking

Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA). These bodies are again part of a broader European multi-layered financial system overseeing financial supervision in the EU.

The last two authorities hold a significant role in the EU's sustainability reporting framework as the European Financial Reporting Advisory Group (EFRAG) and the High-Level Expert Group on Sustainable Finance (HLEG) have both been involved in developing the latest sustainability reporting standards and giving strategic recommendations to the EC. EFRAG also acts as an advisory body for the EC on the endorsement of the International Financial Reporting Standards (IFRS) within the EU. It has also been developing the European Sustainability Reporting Standards (ESRS) and has contributed to the voluntary EU Green Bond Standards (EU GBS). On the other hand, HLEG has been established to develop a comprehensive strategy for sustainable finance in the EU, with a particular focus on EU Taxonomy. The rapid pace of development in sustainability reporting in the EU and the diversity of the underlying objectives and requirements are making it difficult for decision-makers in organizations and researchers to keep track of the changes in legislation and reporting standards.

### 2.2.2 Global scale

On the global scale, table 1 classifies the components similarly to the EU. However, the lack of a single global authority with the mandate to impose and enforce sustainability regulations worldwide means there are no regulation or directives available. One of the main global standards-setting bodies is the IFRS Foundation, under which the International Sustainability Standards Board (ISSB) and Sustainability Accounting Standards Board (SASB) operate. The ISSB was created recently in 2021 to develop a global baseline for sustainability disclosure standards which was previously supported to a limited extent by the SASB standards. In the future, however, the objective is to transition the industry specific SASB standards to the more consolidated ISSB standards. In June 2023, the ISSB launched its two inaugural IFRS Sustainability Disclosure Standards consisting of general requirements for sustainability related financial information (IFRS S1) and more specific climate-related disclosures (IFRS S2). These two sets of standards are built on previous market-led reporting initiatives in an effort to harmonize and streamline reporting processes (IFRS, 2024b).

There is also another framework called the International Integrated Reporting Council (IIRC) established in 2011 which has since merged with SASB and now forms part of the IFRS Foundation through the consolidation of ISSB. In addition to the broad IFRS Foundation, there is the Carbon Disclosure Project, better known as CDP, which offers a complementary approach to the ISSB. While the CDP focuses on environmental transparency and accountability, the ISSB offers a more comprehensive set of standards.

Lastly on the Supervisory and Regulatory Authorities row, we have the non-profit organization called the International Capital Market Association (ICMA) that focuses on the capital markets thus providing guidelines for best practices such as the Sustainability Bond Guidelines (SBG), the Green Bond Principles (GBP) and the Social Bond Principles (SBP). All three are essentially interconnected to provide a unified framework for issuing bonds which is a vital characteristic for any sustainability reporting guideline. The role of the SBG in between the two principles is to combine the recommendations from GBP and SBP in order to provide a holistic approach for green bond guidelines that recognizes both environmental and social projects.

Most independent organizations that offer sustainability reporting standards operate under the same name as their standards. The Global Reporting Initiative (GRI) is one of such that has been widely used by companies around the world. According to a jointly published report in January 2024 by GRI and ISSB their disclosure standards “have a high degree of alignment” (IFRS, 2024a). It is worth noting that while the GRI covers a wide range of sustainability issues, the Task Force on Climate-Related Financial Disclosures (TCFD) focuses on the financial impacts both for companies and financial capital providers. Even though the recommendations of TCFD are voluntary, many jurisdictions such as the European Union and the United Kingdom have implemented them into their regulatory frameworks. Finally, table 1 presents the independent reporting framework created by the United Nations called the UN Guiding Principles Reporting Framework (UN GPFR). This reporting framework is aligned with the global standard of the UN Guiding Principles (UNGPs) and differs from other standards by focusing on salient human rights issues.

Overall, the global sustainability reporting landscape is still fragmented and although efforts to harmonize reporting standards are being made. Throughout recent years, the landscape has been developing quickly and the collaboration between different

supervisory and regulatory authorities is intensive which can be observed from the mergers and consolidations of several standard-setting bodies. According to ACCA's (2016) sustainability reporting landscape analysis, the rapid evolution and inherent complexity of sustainability reporting and its relative novelty have resulted in the lack of a generally accepted framework for expressing and defining different elements of sustainability reporting. Questions have risen regarding the extent and ways in which businesses should address new expectations about corporate performance from NGOs, investors and consumers and they are affecting the way these businesses prepare their reports.

The lack of standardized terminology for defining the components of the sustainability reporting landscape adds to the complexity that currently defines the field. In many cases, regulators develop sustainability reporting requirements to support national policy objectives that can differ globally. Nevertheless, there are intergovernmental organisations such as the Food and Agricultural Organization (FAO), the International Energy Agency (IEA) or the World Trade Organization (WTO) that inform and influence sustainability reporting disclosures. In this case, it is challenging for reporting organizations to comprehend the relationship between the entities issuing the requirements and the objective of the diversity of reporting requirements. The audiences of these reports have expressed frustration with the unnecessary complexity of corporate reports that disguise important information about a company's performance.

There are multiple ways to move forward from this stage. Sustainability reporting is gradually becoming mainstream for companies that cause a material impact on the environment and society. The key driver in improving the overall quality of sustainability reporting is the cooperation between policymakers which entails agreeing on the components of their framework. This can be facilitated by leveraging shared objectives and addressing possible technical differences between institutions. In addition, the role of the private sector and its reporting practices should be discussed. Sustainability recommendations and standards should encourage more environmentally and socially responsible business activities. These activities can enhance the corporate reporting dialogue which has meaningful effects on the financial markets. (ACCA, 2016)

## 3 THEORETICAL BACKGROUND

### 3.1 Underlying theories

The concept of corporate social responsibility is actively evolving as new forms of business challenge our society in unprecedented ways, leading to diverging views between institutions, regulators and companies on how they impact the environment. This raises questions about which practices are genuinely socially responsible. There are various theories trying to explain the ethical nature of corporate social responsibility and the behaviour of firms in the new sustainability landscape. To facilitate a better understanding of firms' responses to external challenges (i.e., CSRD), this study integrates three theories in separate sections.

Stakeholder theory and legitimacy theory have their roots in the broader political-economic theory perspective (Deegan & Blomquist, 2006; van der Laan, 2009). Although both theories focus on the relationship between an organization and its operational context (Neu et al., 1998), they exhibit different characteristics. Legitimacy theory, for instance, revolves around "perceptions and the processes involved in redefining or sustaining those perceptions, and can accommodate notions of power relationships and discourses at a global level" (Moerman & Van Der Laan, 2005). On the other hand, stakeholder theory is considered the more appropriate approach for explaining managerial conduct concerning engagement with specific stakeholders, such as financial institutions. These two theoretical frameworks should not be perceived as entirely separate and isolated; instead, a more appropriate way to view them is as intersecting perspectives situated within the framework of assumptions underpinning the "political-economic perspective" (van der Laan, 2009).

A substantial body of prior literature has primarily addressed ESG reporting using the lenses of legitimacy theory or stakeholder theory (Chelli et al., 2014), although some researchers argue that there is a third, signalling theory that anticipates a considerable loss of trust among financial market participants as a result of persistent inconsistencies between a firm's promises and actions (Merkl-Davies & Brennan, 2007). Rodriguez-Fernandez has also identified agency theory as a prominent theory in corporate sustainability reporting due to the possible conflicting views of the board of directors and the company's shareholders. It remains unclear who should be held accountable for

socially responsible activities that may or may not increase shareholder value. (Rodriguez-Fernandez, 2016)

In the theoretical framework of the signalling theory, the role of investors is emphasized as the main audience for reporting disclosures. This can be regarded as an opposing view to the socio-political theories that study the information asymmetries between the firms' inside and outside stakeholders. According to Adams and Frost (2008), both perspectives should be examined in order to obtain the full scope of the impact and role sustainability reporting has not only in corporate investment decisions but also in stakeholder engagement. (Adams & Frost, 2008; Merkl-Davies & Brennan, 2007)

### 3.1.1 Stakeholder theory

Stakeholder theory presents a holistic approach to address relevant investors and other parties that have stakes in the company by active communication and supportive actions towards all demands received. The theory analyses and classifies different groups, identifying those that justify managerial focus according to established criteria, and distinguishing them from those that do not require such consideration. These groups are ranked in order to prioritize the interests of stakeholders to whom the company might be held accountable and is therefore necessary to report its activities. (De Silva Lokuwaduge & De Silva, 2022)

The theory recognizes the power that stakeholders have over a firm's actions, but at the same time the firms have leverage between environmental communication and organizational outputs. Disclosures tend to highlight environmental actions, reformulate challenges presented by key audiences and ignore those raised by marginal audiences. (Neu et al., 1998.) Organisations need to be able to solve conflicts between their stakeholders which is why having reliable environmental performance indicators is crucial for them. Even though the new EU directives aim to provide better guidance for quantifying environmental issues, some researchers believe there is still plenty of room for management discretion. (Velte, 2023)

From a stakeholder theory perspective, a firm is conceptualized as a nexus of various stakeholders, encompassing individuals and groups who maintain essential relationships with the business. These stakeholders, through their interactions and interests, significantly influence the firm's operations and strategic direction which has mutual

benefits. As value creation is the core objective of a business, the stakeholder network becomes an essential tool that maintains a functioning value creation pipeline. Without proper support from external and internal stakeholders, the business' future operations will be compromised. The basis of a company's operations derives from a common vision with its stakeholders that is favourable for joint value creation. (Edward Freeman, 2010.) According to Birte et al. (2020), if the joint value creation is not mutually beneficial for all parties, the business will lose its partnerships and resources thus eventually becoming redundant. It will also lose its legitimacy which has originally given the business the ability to build relationships. It fundamentally means that a company is created to produce value not just for its stakeholders but also with them. (Birte et al., 2020)

Value creation raises the question of its definition, which varies depending on the recipient. Individuals have different views of what value is, hence, in the broadest sense, value is created when it meets an entity's personal or professional needs. Stakeholder relationships are nuanced because they all vary in their contribution and definition of value creation. Birte et al.'s stakeholder value creation framework addresses the widely conceptualized idea of a unidirectional value flow and replaces it with a more appropriate, circular-shaped framework. This perspective provides a clearer understanding of value streams and a more robust foundation for developing sustainable business models. Being able to manage the stakeholders' input is key to finding innovative solutions to improve the society. (Birte et al., 2020)

### 3.1.2 Legitimacy theory

Legitimacy is an essential tool for businesses to be able to operate in modern society. Companies that lack legitimacy may feel lost, because legitimacy measures the significance that businesses have in our society. According to legitimacy theory, companies have social contracts that include social obligations that they must respect (Shocker & Sethi, 1973). Firms risk their operational continuity if their actions do not comply with society's environmental regulations, such as the UN climate change policies. To avoid scrutiny about legitimization, Velte suggests implementing an environmental management system that supports more comprehensive environmental performance indicators. This sort of legitimization strategy helps withstand demands from stakeholders that expect additional environmental reporting on top of the mandatory financial reporting measures. (Velte, 2023.) ESG reporting is considered a mechanism which allows

companies to manage their legitimacy and societal reputation and various multinational businesses have developed organisational strategies to justify their operations by committing to more sustainable processes (De Silva Lokuwaduge & De Silva, 2020).

Mahoney et al. (2013) have argued that there is a risk of saturation of sustainability reporting data which can contribute to greenwashing but also lead to increased legitimacy. Thus, environmental performance and environmental reporting might not always be positively correlated but also negatively correlated which lacks tangible significance (Velte, 2023). Impression management, where the top management aims to influence external stakeholders to perceive the firm in a certain way, is commonly used as a response to public pressure (Merkl-Davies & Brennan, 2007). To reduce this type of behaviour, legitimacy theory suggests that the right board composition and ownership structure can discourage the top management from similar greenwashing actions or even motivate them to act more transparently (Velte, 2023). Institutions form an important body that puts pressure on enterprises concerning ESG issues (Tate et al., 2010). Companies are trying to take advantage of these legitimacy benefits by gaining access to the Dow Jones Sustainability Index where companies are labelled as sustainable businesses (Cho et al., 2014).

According to Tilling (2004), legitimacy theory provides a way to understand why and how enterprises are involved in social and environmental reporting. The legitimacy of an organisation shapes the expectations that the public has according to how it is perceived by external stakeholders and society (Tilling, 2004). This implies that organisations must also consider the interests of society besides their own investors. Many researchers often apply legitimacy theory to explain why corporate managers take certain actions such as publicising ESG information as a part of their corporate strategy. (De Silva Lokuwaduge & De Silva, 2020.) However, it is not suitable for offering a prescribed formula that might reflect the top management's way of thinking. It is a theory that rather seeks to explain the behaviour of such managerial activities. (Deegan, 2014.)

### 3.1.3 Signalling theory

Signalling theory and agency theory both deal with information asymmetries and reflect the relationships between different shareholders of a firm (Arrow, 1985). Sustainability reporting is an essential instrument for companies and financial institutions to use not only for compliance purposes, but also to signal to investors that they are actively

committed to sustainable development, such as by redirecting capital into innovations that promote sustainability (Clarkson et al., 2019). According to signalling theory, increased awareness of SDGs incentivizes corporations to engage in voluntary assurance, especially in sectors that are environmentally friendly, since they usually have more positive information to communicate than environmentally harmful ones (Elalfy et al., 2021; Krasodomska et al., 2023; Sierra García et al., 2022). Thus, the signalling theory plays a vital role in how firms decide to manage their reputation. It is a multifaceted issue that has long-term impacts on the organisation's value, financing alternatives, and other elements. (Matsumura et al., 2014; Plumlee et al., 2015.)

Clarkson et al. (2019) have also made an interesting argument in their research paper about the globally recognized GRI sustainability standards arguing that they still leave a lot of room for managers to implement disclosing strategies while following these guidelines. Nonetheless, KPMG issued its sustainability study in 2022, and the proportion of the world's biggest 250 corporations by revenue (also known as the G250) that have embraced TCFD's disclosure requirements nearly doubled in two years, from 37% to 61% (KPMG, 2022a). This shows that there is a rising awareness of climatic, societal, and governance concerns. Corporations understand the value of independent assurance for achieving transparency and accountability for their sustainability reporting. (Clarkson et al., 2019)

Signalling theory suggests that the top management has the option to mitigate the inevitable information asymmetry between the company and its stakeholders (Merkl-Davies & Brennan, 2007). It is their method to signal their commitment to sustainable matters and increase their credibility among investors by listening to their concerns (Krasodomska et al., 2023). The theory also notes that the more ESG friendly and profitable a company is, the more effort it will put into ESG reporting resulting in higher-quality sustainability reports. Investing in sustainability matters is costly, which is why larger corporations are often the first to act and smaller organizations follow once they successfully implement new measures. (Clarkson et al., 2019; Neu et al., 1998.)

## 3.2 Reporting requirements for financial institutions

### 3.2.1 Sustainability risks in voluntary and mandatory sustainability reporting

Recent studies have yet to come to an agreement on whether mandatory ESG reporting has proven to be a more effective tool than voluntary ESG reporting in reducing information asymmetry between companies and investors which translates to a more accurate perception of the company's valuation (García-Sánchez et al., 2023). To address the increasing demand for enhanced ESG disclosures by companies, regulators across various jurisdictions have implemented diverse regulatory measures, encouraging organizations to incorporate ESG data into their annual reports. Several countries have mandated the disclosure of ESG-related information within conventional annual reports or in separate ESG reports. Other countries have established voluntary standards to assist organizations in measuring, comprehending, and conveying their exposure to ESG risks and opportunities. (Cicchello et al., 2023.) In certain instances, there is no mandatory regulation, and non-financial reporting efforts are primarily focused on socially responsible companies or those that seek to adhere to stakeholder demands (Krueger et al., 2023).

Given these arguments, previous studies have found that the decision to require mandatory disclosure of non-financial information may fail to improve the quality, reliability, comparability and performance of disclosures. The Italian literature has addressed the subject extensively which may help the comparison of results due to the geographical limitations of the data, which reduces some variables of the study (Tarquinio et al., 2020). A study conducted by Agostini et al. (2022) investigated 20 Italian companies two years prior and after the NFRD's implementation to evaluate if the regulatory changes made any difference between non-financial disclosures and corporate financial performance. Their findings show that the new NFRD had a positive effect on the quantity of sustainability reports but did not significantly enhance the quality of the reports (Agostini et al., 2022). However, opposing viewpoints from Italian case studies suggest that the increase in regulation may actually be a constraint on business proactivity (Tarquinio et al., 2020).

The European Union's Sustainable Finance Disclosure Regulation describes a sustainability risk as "An environmental, social or governance event or condition that, if it occurs, could cause an actual or a potential material negative impact on the value of the

investment”<sup>1</sup>. For investors, any risk that could influence company valuation is being considered. In recent years, they have begun to employ ESG information in their investments, shifting the focus away from traditional finance. Sustainability has introduced a new dimension to the fundamentals of the organization, which is interconnected with investments. (Peylo & Schaltegger, 2014.) ESG risks are not only systemic to the global financial system, but also for long-term value creation. Although it is not meaningful to define a monetary value to biodiversity, several studies conducted by central banks found out that around 35-54% of global assets held by financial institutions rely on services provided by ecosystems. (OMFIF, 2022)

In 2021, the U.S. Financial Stability Oversight Council addressed climate change as an increasing threat to the country’s financial stability which will have a toll on the global GDP with current policies (Nordea, 2023). Accurately identifying and translating biodiversity threats into business-impacting economic hazards is currently one of the largest issues confronting enterprises. Enabling financial markets to appropriately include the worth of biodiversity and the danger of its degradation in financial analyses and risk mitigation strategies is fundamental. The impacts and dependencies of biodiversity are being evaluated through the rapid evolution of data, measurements, and early scenarios; yet these tools are insufficient to accurately evaluate the financial risks associated with biodiversity. To effectively guarantee that biodiversity risks are incorporated into financial organizations' risk management, the outcomes of biodiversity effects and interdependencies must be converted into metrics that can be taken into account alongside financial choices. (OMFIF, 2022)

At a company level, strong ESG risk management throughout the value chain may result from top management fostering a culture in which sustainability is viewed as both a possible risk area and an economic driver. This can then stimulate long-term innovation and strengthen a company's reputation. (Nordea, 2023) Consequently, regulations on sustainability disclosures include a provision that allows firms to either comply with increased ESG disclosure requirements or explain their reasons for not doing so. Therefore, if firms perceive that the costs associated with disclosure—such as those related to proprietary information, preparation, or political implications—are too high,

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<sup>1</sup> Regulation (EU) 2019/2088 Of The European Parliament And Of The Council Of 27 November 2019 on sustainability-related disclosures in the financial services sector, Article 2 (22).

they might choose to avoid disclosing the data and instead justify their decision. (Ioannou & Serafeim, 2017.)

Gerwing et al. (2022) note that companies employ a range of voluntary sustainable corporate governance mechanisms, in addition to mandatory audits, to enhance the quality of their mandatory sustainability reporting. Key mechanisms for mitigating sustainability risks include sustainable remuneration for the executive board, the establishment of CSR committees, participation in CSR initiatives, and obtaining external assurance. Overall, firms have various voluntary practices at their disposal to manage sustainability risks effectively. Moreover, mandatory sustainability reporting can help reduce information asymmetries between company managers and stakeholders, which might otherwise hide crucial sustainability information. (Gerwing et al., 2022)

### 3.2.2 Implementing sustainability in the banking sector

Banks may not be directly involved in social and environmental disasters, but their actions are crucial in supporting initiatives supported by other sectors or banks. The most significant social and environmental activities are most often linked to banks that finance or otherwise support sectors or campaigns. They are therefore a driving force in the research and development of ESG (un)friendly products. This makes the financial sector crucial to the growth and progress of environmental sustainability and corporate social responsibility. Banks, in particular, aim to address social needs to establish a strong local foundation for future sustainable business (Nizam et al., 2019). Thus, the financial sector plays an instrumental role in influencing the social and environmental behaviour of other sectors, especially their creditors. (Douglas et al., 2004)

The banking industry is essential to advancing the green revolution and maintaining the planet's ecological sustainability. Banks contribute significantly to initiatives that assist green development and environmental integrity through their strategic position. Among them are the offerings of sustainable bonds, green bonds, and green loans. These financial tools are intended to support green initiatives including solar energy development, eco-friendly construction, and the development of renewable energy sources. The banks' financial support of these projects matters since it makes it possible for them to be completed, which benefits the planet's well-being. (Miah et al., 2021.) Moreover, banks can impose opposite measures such as sanction mechanisms to adopt green technologies. For instance, banks offer financial services to a variety of sectors, including cement,

chemical, clothing, and paper industries, which are significant carbon emitters. By setting higher costs on similar projects that pose environmental threats, banks can work to reduce the carbon footprint of these industries. (Miah et al., 2021.) Nieto (2017) estimates that banking systems in the US, EU, China, Japan, and Switzerland have collectively allocated an impressive 1,6 trillion US dollars in loans to sectors with high environmental risks, such as oil and gas, power generation, and automobiles. Policymakers and regulators are increasingly interested in exploring how banking institutions can develop greener financial services for these markets. However, the current discourse largely focuses on developed nations, while the vulnerabilities of developing countries remain significant and must not be overlooked (Ihlen, 2009; Kolk & Pinkse, 2005).

Clients that are looking to support companies with good corporate responsibility through investments need to be able to analyse these companies from an array of perspectives to get an idea of not only their ability to generate future earnings but also to know what kind of impact the company is making to society (Nordea, 2023). They have begun to rethink their environmental impact and consider the ramifications of their behaviour on society. Companies are forced to do the same and change their strategies in order to maintain their competitive advantage over new market participants that are using these issues to try to set themselves apart. (Aich et al., 2021) Clean technologies can establish a market niche, allowing banks to profit by expanding into untapped markets. Consequently, banks should, in their own interest, take comprehensive steps to assess the extent to which a project might contribute to climate change. (Miah et al., 2021.)

As banks strive to regain their credibility after the recent banking turmoil in the EU and the US and enhance their financial stability, it is essential for them to integrate sustainability into their operations both promptly and strategically. This integration should encompass internal practices within the banks, such as their own operational processes, as well as external practices, including their financing and investment portfolios, and their interactions with clients and communities. (Nizam et al., 2019.) There are multiple studies confirming excess returns on portfolio strategy and investment analysis when integrating sustainability factors (Auer & Schuhmacher, 2016; Nagy et al., 2015), but that does not necessarily lead to an increase in banks' business performance. To achieve this, Khan et al. (2016) suggest that banks should integrate material environmental and social indicators into their business models, ensuring access to high-quality data. Materiality is crucial in the banking sector for assessing sustainability

performance because, without accurate identification of material factors, effective analysis of sustainability impacts is impossible. Hence, identifying the relevant factors that influence banks' performance is essential. (Nizam et al., 2019)

A study conducted in the global banking sector investigating the association between CSR and financial performance found out that the motive driving banks to engage in CSR affects their financial performance. The evidence revealed that out of the three motives analysed, strategic, altruistic and greenwashing, the predominant motive that generated positive net and non-net interest incomes, as well as net profits, was strategic. Altruistic banks resulted in an increase in net and non-net interest income although the increase in net profits was inconclusive. (Wu & Shen, 2013.) Another study from 2016 that examined U.S. commercial banks revealed that larger sized banks outperformed smaller ones until the financial crisis in 2008. Consistent with these findings, banks with higher capital ratios, greater profitability and lower fees tended to be more ESG-friendly. This may be attributed to the fact that larger banks have more resources to invest in sustainability initiatives and report these activities to their stakeholders. (Cornett et al., 2016.)

These promising studies along with opposite evidence from others (Chih et al., 2010; Nollet et al., 2016) showcase the complexity of producing truly robust results of CSR impacts to financial performance. Researchers have the possibility to select studies that support their hypotheses to increase the credibility of their own results. There is also the problem of the methods and models they use. Sustainability remains difficult to quantify, so limiting the study to certain aspects can introduce unwanted biases into the results. Thus, the banking sector is missing more recent studies in this area of research that take into account the issues mentioned above.

### **3.3 Sustainability disclosures in the food industry**

The growing concern about the dramatic increase in the world's population has seen food industry participants take steps towards more sustainable practices. A report published by the United Nations (UN) announced that the world population is expected to reach 9,8 billion in 2050 (United Nations, 2017). Such an increase will have implications specifically in the food sector which has to produce enough food to meet the needs of the human population (Buallay, 2020). As a result, sustainability is more necessary than ever due to its environmental and social impacts. The food industry is a dynamic business environment with high customer expectations for food safety and a growing demand for

sustainably produced food (Beske et al., 2014). Up to 81% of consumers urged that the food sector should pay greater attention to sustainability, which is why many firms in the sector have begun to embrace sustainable practices and report on them in their sustainability reports (Ihlen et al., 2011; Wurth, 2014). Thus, food companies are becoming more transparent on their sustainability efforts (Rankin et al., 2011).

The extensive nature of the agricultural sector, which includes a wide network of businesses and stakeholders such as farmers, food producers, retailers and suppliers, makes it challenging to accurately assess the value proposition of sustainability reporting for individual organisations (Buallay, 2021). A few studies analysing the Spanish agri-food sector have found a similar trend of low disclosure levels in companies operating in the sector which supports the previous argument (Anguiano-Santos & Rodríguez-Entrena, 2024). The same industry is intrinsically characterized by its significant consumption of water and energy, thereby casting doubts on the dedication of corporations towards sustainable practices. Moreover, the Banco Mundial (2021) has documented that this sector accounts for roughly 33% of carbon dioxide and other greenhouse gas emissions, thereby underscoring the imperative for enhanced transparency and accountability in environmental matters.

Agri-food companies operate with different levels of sustainability depending on what factors influence their sustainability strategies (Grolleau et al., 2007). Factors such as customers, governments, the media and even the position of a company in the supply chain influence the stance companies take in their sustainability efforts. Previous literature has identified five stages of sustainability, ranging from compliance and profit-based approaches to sustainable innovation, organisational and societal perspectives. A study by Rankin et al. analysing a sample of US agricultural executives found that among these sustainability levels, external pressures such as government, media or competitors had little influence on corporate sustainability actions. (Rankin et al., 2011)

The sustainable food industry is constantly influenced by evolving customer perceptions and expectations. This evolution is driven by frequent NGO reports highlighting environmental issues like deforestation and social concerns such as fair wages for farmers. (Hassini et al., 2012.) By integrating sustainability into their supply chains, food companies can alleviate external pressures from stakeholders. Both academic research and practical applications of sustainable supply chain management have demonstrated

that the globalization of food supply chains has fostered dynamic capabilities, enhancing the overall sustainability performance of the supply chain. (Beske et al., 2014.) The CSRD puts the European Union as a global leader in advancing supply chain sustainability, aligning with its goal to decarbonize the economy. It mandates that companies disclose information not only about their own operations but also about their upstream and downstream supply chains. As a result, companies are required to allocate more resources to managing relationships with suppliers and to incorporate sustainability-related risk assessments into their procurement processes. (Deloitte, 2024)

The dynamic capabilities identified by Beske et al. (2014) highlight opportunities for companies to actively manage and develop their supply chains in a sustainable manner. Achieving transparency in sharing information throughout the supply chain and the willingness to develop partnerships are crucial components of this process. Partnerships should not only be formed with supply chain partners, but also with government and non-governmental organizations (Elkington, 1997). The lead companies of their supply chains may provide training for their suppliers to enhance their understanding of environmental issues and promote responsible practices (Ras et al., 2007; Wiskerke & Roep, 2007). Socially, this would involve ensuring that codes of conduct are implemented and monitored. On the operational side, increased transparency facilitates tracking and tracing efforts, which are crucial for addressing food scandals and complying with legal requirements. (Beske et al., 2014)

Studies on performance measures in supply chains recognize the challenges involved in creating reliable metrics, with some of these challenges being intrinsic to the nature of supply chain management (Hassini et al., 2012). According to Hervani et al. (2005), selecting appropriate environmental indicators and reaching a consensus on these metrics with various supply chain participants presents significant difficulties. Additionally, Bendoly et al. (2007) discovered that aligning strategies across the supply chain and coordinating the skills of different parties can lead to redundancies.

In summary, incorporating CSR as part of business strategy and differentiation, along with integrating its disclosures in food supply chains, can lead to more transparent and efficient vertical relationships. Enhanced efforts to collaborate with supply chain partners on preventing and managing environmental impacts, as well as increased monitoring

costs to gather stakeholder feedback, play a crucial in improving coordination among supply chain members. (Stranieri et al., 2019)

For instance, Stranieri et al. (2019) provided an example where implementing procurement standards or changing supplier selection methods illustrates how food companies are adapting their practices to comply with CSR regulations. This indicates that supply chain partners are creating closer relationships to mitigate behavioural uncertainties that arise from increased interdependencies. Therefore, the integration of CSR in food supply chains not only promotes transparency but also strengthens partnerships, leading to more sustainable and resilient supply chain practices.

### **3.4 Debt financing and sustainable finance**

#### **3.4.1 Debt financing as a sustainability driver**

Historically, the perspective on corporate governance has primarily centred on the roles and interests of shareholders and directors, often overlooking the significance of creditors. This traditional viewpoint is evident in the emphasis placed on equity as a primary vehicle for shareholder activism and involvement. Nonetheless, private debt instruments, such as loans and bonds, represent a considerable segment of the resources that corporations utilize for financing their activities. These debt mechanisms provide a unique array of legal avenues through which to impact corporate behaviour. Consequently, the discourse within corporate law and financial regulatory studies is progressively recognizing the importance of creditors in the governance of corporations. (Park, 2019)

Such debt instruments play a critical role in the progression of economic development, and it is reasonable to anticipate their impact on environmental matters as well (Gylfason, 2001). A mature financial system leads to the establishment of market interest rates that accurately represent the appeal of various financing options. Moreover, advanced financial systems enhance the company's capacity to manage risks associated with unexpected events, potentially contributing to societal stability. (Scholtens, 2006)

Projects related to the environment, governance and social issues can be supported through various financial instruments, such as shares issued by companies (i.e. shares in listed companies) and debt securities (e.g. bonds) (Inderst et al., 2012). Debt has been

largely ignored as a control mechanism to influence the behaviour of firms. However, the legal order of priority gives creditors priority over their shareholders, which in turn has led to the assumption that they value less than shareholders the right to vote and the protection of trusts under company law (Schwarcz, 2016). However, this debt-based management approach has weaknesses. The covenants in listed bonds are weakened by the large number and fragmentation of bondholders, while credit default swaps discourage lenders from exercising their leverage over borrowers. This is because they have the right to transfer the risk of default to a third party (Yadav, 2014). Thus, there are structural concerns that must be addressed when funding ESG related ventures, particularly bond related implications that are currently understudied (Park, 2019).

### 3.4.2 ESG as an investment factor

At times, the concept of ESG integration is broadly interpreted to represent the entirety of responsible investment practices. However, the methodologies and expectations surrounding ESG integration have evolved considerably in recent times. The absence of a standardized methodology for implementing ESG integration means that approaches differ significantly among various investors and across different asset categories, as noted by Eurosif in 2018. Such diversity in application leads to varied outcomes regarding the effectiveness of ESG strategies, which is largely dependent on the investor's execution of these strategies (Busch et al., 2016). Eurosif (2018) further elaborates that the spectrum of ESG integration techniques ranges from minimal, checkbox-style approaches to comprehensive strategies that are seamlessly woven into the entire investment process.

In a discussion that took place in 2016 at the SASB Symposium, a number of professional investors from different fields found a consensus concerning the positive impact of ESG factors on successful investments. They noted that the increasing regulation that ESG is having, should provide higher reliability to ESG reports since the need to rely on regulation decreases. ESG data can be categorized as low-frequency and high-frequency data and the difference between the two is remarkable, since ESG data since reports are usually published annually. Individual investors should recognize the difference from financial data, which is usually reported in high frequency, as the two categories are not necessarily consistent when comparing them. That being said, ESG metrics are still a fundamental part of financial analysis for the world's best value investors such as Warren Buffet. (Hanson et al., 2017)

As the number of institutional investors using ESG issues in their investment strategies grows, there is still mixed empirical evidence on the benefits of corporate social responsibility alongside CFP (Corporate Financial Performance). Zahid et al. have studied the critical role of the audit quality of this relationship stating that most researchers have ignored or overlooked the importance of audit quality in their studies. Previous models focusing on the association between corporate social responsibility and financial performance are not robust, thus forgetting to take into account other factors such as organizational behaviour or growth performance that are equally as important. (Cho et al., 2019; Zahid et al., 2022)

As a result, the empirical results from studies analysing this issue can hardly be divided into two camps. Although some academics have found a positive relation between CSR activities and CFP, and others argue the impact of CSR has a negative effect on the earnings of a company. There are a few studies that even find the correlation between the two to be non-existent. (Cho et al., 2019.) The reason for not having consistent results lie in the imperfections and differences of these studies. Margolis and Walsh concluded that there are alternating views among researchers on which variables should be used in the creation of models which conversely causes the omission of other variables, changing the outcome of the models. The lack of identifying the causality in the regressions and not being able to adequately base the results on theory has also skewed the results. This evidence comes from a review of 127 studies on the relationship between social corporate initiatives and financial performance between 1972 and 2002. (Margolis & Walsh, 2003)

To confirm the hypothesis that responsible companies outperform their peers, the dataset needs to be as broad and reliable as possible. There are studies like the one from Choi et al. (2010) that have observed a positive impact on the effect of social responsibility to company performance when analysing data of companies from 2002 to 2008. In the study the data was obtained from the KEJI index which is used to measure financial and CSR performance in Korean companies listed in the Korea exchange. The models used were robust, containing three variables that measure operational performance (ROA), financial performance (ROE) and market performance (Tobin's Q). A comprehensive analysis was performed using different sample groups in order to balance the importance of stakeholders in different firms. Additionally, further bi-directional analyses were made to address the causation between CSR and corporate financial performance. (Choi et al., 2010)

The results show that there is a positive link between corporate financial performance and corporate social responsibility, although it is dependent on the primary stakeholders of the firm. The findings suggest that firms must first identify their primary stakeholders and then target the right social initiatives that will benefit those stakeholders. (Choi et al., 2010.) Buallay (2018) performed similar analyses using the same three dependent variables in the context of the European banking sector. However, her empirical findings led to somewhat ambiguous results, as her regression analyses produced inconsistent results depending on whether the ESG indicators were used in the same model or separately. Only environmental disclosures were found to be positively correlated, whereas corporate social responsibilities and governance disclosures had mainly a negative effect. (Buallay, 2018)

Recent studies have taken into account environmental issues more profoundly, which were not as important in the past. The studies have shown that there is a more complex relationship between ESG and financial performance than just a simple linear correlation which opens up a new research gap. (Zahid et al., 2022.) A large body of literature finds environmental regulation to be financially harmful for companies even if they are awarded for their “green” contributions. Environmentally and socially friendly actions are costly, and companies often are not very keen on implementing measures that are not financially favourable. If tensions between the demands of shareholders and the pressure from secondary stakeholders arise, the company may have the incentive to exaggerate its accomplishments to satisfy both needs. (Eun-Hee & Lyon, 2015). Other studies have come to the same conclusion based on evidence that companies with high social and environmental corporate spending are more vulnerable to financial losses. (Chon & Kim, 2011)

Information disclosure strategies or in other words, “greenwashing” or “brownwashing” have been effective tools for companies to exaggerate their sustainability accomplishments. While greenwashing relates to environmental performance, brownwashing is used to reflect the social and governance actions of a company. Corporations under corporate sustainability regulatory frameworks use different disclosure methods in order to report their actions according to their needs. When the firm is in a growth phase, it tends to overestimate its sustainability actions in order to construct a solid reputation thus improving stakeholder interactions. On the other hand, if the firm is struggling to make a profit while the pressure from investors is rising, it tends to

understate any commitments made toward environmental, social and governance topics.  
(Eun-Hee & Lyon, 2015)

## 4 RESEARCH METHODOLOGY

### 4.1 Research design

The methodology for the case study is a qualitative method by interviewing key stakeholders in the food industry and financial market participants in that industry. An interview is essential for this topic as the research area is still relatively new and there is not yet enough good-quality data available for statistical research. The interview will be conducted on a semi-structured allowing for follow-up questions in order to enable more in-depth discussions, but at the same time the interview still remains in a formal setting with predetermined questions. The main goal of the interview is to find answers to the research objectives. Moreover, the interview serves as a tool to gather information from experts in the financial industry and also to identify the personal views of financial experts on ESG awareness, investment decisions and stakeholder insights. During the interview and while handling data, principles of research ethics will be followed.

Qualitative methods involve interpretation, while quantitative methods rely on hypothesis testing and statistical analysis. Qualitative research is likely to be exploratory and is particularly useful when there is little prior knowledge of the problem. Case studies often use a qualitative approach to assess and understand the situation (Eriksson & Kovalainen, 2008). This study aims to explore a new phenomenon and gain insights from the perspective of external stakeholders. Therefore, a qualitative method was assigned for this case study.

A case study serves as a way to explain the depth of a complex issue in a more approachable way. The practicality of the study provides detailed insights into the studied phenomenon in a real context. (Farquhar, 2012.) The case study technique has also been criticized for its lack of scientific integrity. Therefore, many business case studies are practical which is why this thesis intends to discover relevant answers to research questions and subjects based on prior literature (Eriksson & Kovalainen, 2008; Tuomi & Sarajärvi 2018).

## 4.2 Data collection

### 4.2.1 Interviews

The primary source of data will be collected from the semi-structured interviews. According to Saunders et al. (2009) semi-structured interviews are used to understand the meaning and explanations of concepts. The interactions in a semi-structured interview should be allowed reasonable time so that answers can be elaborated. Personal views were left out during the interview so that they do not oppose the perspectives of the interviewee thus changing the course of the interview. (Saunders et al., 2009)

The interview selection process was initially carried out through the business-focused social media platform LinkedIn. Its premium feature is ideal for contacting target individuals since LinkedIn enables quick screening of suitable profiles for the research and the recipient's response rate is often higher than that of email. In any case, conversations eventually moved to emails where, among other information, it is more practical to share the privacy notice and meeting details. For the interviews, 16 ESG professionals were found who fit the profiles of potential interviewees for the data collection part of the research. This represents an acceptance rate of around 38% of interview requests.

### 4.2.2 Data collection and analysis

The data management follows the University of Turku's guidelines. Interviews are recorded with prior consent from the interviewees. These recordings are solely for research purposes and accessible only to the author. Interviewee anonymity is maintained throughout the research process, and they have the opportunity to review the interview translation afterward. By providing interviewees with the opportunity to review their responses, the research process remains participatory and respectful of the contributors' input. The data management plan, which outlines the procedures for data storage, access, and confidentiality, is available in Appendix 2. This plan includes specific measures for safeguarding the data and ensuring compliance with ethical standards. These ethical considerations are discussed further in section 4.3.

All interviewees together represent different perspectives from financiers on sustainability-driven lending. Each of them has a different background in the financial

sector on working with sustainability issues, and together they form a diverse target group that takes into account as comprehensively as possible the perspectives of financial institutions in financing sustainable development. The interviewees' work experience varies from smaller private companies and publicly listed companies to private equity companies and consulting firms all based in Finland. In total, six interviews were conducted between February and March 2024 by video call via Microsoft Teams. The interview questions can be found in Appendix 1 in English although the actual interviews were conducted in Finnish as it was the preferred language for the interviewees. It should be noted that while the intention of the researcher is to accurately preserve the original meaning of the responses, the translation of the data may still result in some minor changes to the underlying meanings. After the interviews, the data is automatically transcribed by Microsoft Teams using its embedded transcription feature. Additionally, the recordings were transcribed again using the University of Turku's own transcription service called the UTU Transcribe Service, which utilises artificial intelligence to ensure the most accurate results. This dual transcription approach maximizes the accuracy of the script, allowing any ambiguities in the answers to be cross-checked with either the other transcript or the original recording.

Table 2 Overview of interviews

Interviewee	Role	Interview date	Interview duration
1	Director of Sustainability Services and ESG	19.02.2024	34min
2	Senior ESG Specialist	22.02.2024	31 min
3	ESG and Sustainability Expert	23.02.2024	50min
4	Director of Legal, Tax and ESG Affairs	05.03.2024	36min
5	Group Executive for Sustainability and ESG	07.03.2024	25min
6	Competition Law and Sustainability Director	13.03.2024	33min

Table 1 presents an overview of the participants which categorises them according to their professional role. The interviewees were informed of the measures taken to anonymize their contributions in the dissemination of findings, with the intention of augmenting the sincerity of their responses. Each participant expressed their willingness to be cited within this research, irrespective of the necessity for explicit approval pertaining to specific

quotations. On average, the duration of the interviews was approximately half an hour, with the most extended session lasting 50 minutes and the briefest spanning only 25 minutes, attributed to the constrained timetable of the interviewee. All discussions were recorded and subsequently transcribed, producing a script of 35 pages with a font size of 12 and spacing of 1.

### **4.3 Research ethics**

Ethical considerations hold significant importance in research, especially in studies involving primary data collection from human subjects. This study adheres to the ethical principles for research in the humanities, and social and behavioural sciences outlined by the Finnish National Board of Research Integrity (TENK, 2012). All participants in this research provided informed consent before their involvement. They were informed about the purpose and goals of the study and were allowed to request additional information about the research at any point. To address concerns regarding sensitive information, this study ensures the anonymity of interviewees and the case companies involved. However, achieving absolute anonymity in a case study presents challenges, as it would render the methodology akin to that of a questionnaire-based study (Eskola & Suoranta, 1998). It's important to note that this research does not delve into the personal information of the participants or critical business secrets.

## 5 RESULTS

The results of the empirical study are presented in this section. The outcomes are all based on primary data from the interviews. The section is structured as follows: There are three main chapters in which the results are classified into three themes, which is a systematic method of deriving themes from the data that illustrate the research problem (Eskola & Suoranta 1998). The themes were created based on the research questions of the thesis and then further elaborated based on the content of the interview answers. Each chapter provides a more in-depth analysis of the responses to that theme, while offering original quotes to enrich the discussion. These extracts from the interviews conducted are used to present the opinions of professionals on the subject, so that their views can be properly conveyed. The findings of the study are analysed using a thematic method of evaluation, which is more common in a deductive research approach. The framework established on the foundation of the literature mainly guides the implementation of the themes and structure, which together with the results constitute the main contribution of the work. Section 6 further discusses the results of the cross-sectional analysis with reference to the theoretical framework.

### 5.1 Sustainable finance and auditing

The interviews started off by discussing disclosure regulations for financial institutions and how the CSRD affects them. The first sub-section focuses on the first research question, which is also related to SFDR requirements for financial institutions. This theme relates to understanding the necessary changes needed to make in order to adapt to the new flow of information that will be available from the CSRD based reports. Auditors have also a key role in the legitimization of sustainability reports since financial institutions rely on the provided material made by them to further analyse how environmental, social and governance targets are met. The CSRD will increase the need for companies to collect more data on their own operations and on value chain activities. Interviewee 1 summarises it as follows:

The first thing is that whatever the goal, there is a shocking need for new information about your own operations, those of your partners and companies up the value chain. It usually boils down to two things, the first of which is the carbon footprint. This relates previously to your own company and its operations, but now it also relates to the firm's products and what they will do over their entire life cycle. The second is climate risk, so we are talking about

physical risks, but also risks related to transition. So, if a company has a product, will it still be relevant in ten years' time when the market changes to a low-carbon world? (Interviewee 1)

Another interviewee reflects on the changes through their own process, although CSRD reports do benefit the company when seeking financing.

We do not currently have a CSRD reporting obligation, but we will find out if the company is subject to NFD reporting or CSRD obligations. We also have certain ESG criteria or cutoff criteria if there are significant environmental impacts. In such cases we ask for a statement on the company's sustainability and then, for example, CSRD reporting would support the company's eligibility for funding. (Interviewee 6)

Interviewees 2 and 5 also raised the importance of data harmonisation, where companies will report in a standardised way according to the EU Taxonomy Regulation, which will improve the comparability of data and thereby highlight, through the dual reporting requirement, what are ultimately the most important issues. It should result in a win-win situation since companies such as Valio, will receive more precise information from their supply chains that will make it easier to manage the whole supply chain. Overall, the consensus among interviewees is still that the actual CSRD reports are still expected to be published from 2025 onwards, making it difficult to accurately assess their impact on sustainability reporting in general.

The quality of such sustainability reports is perhaps as important as the actual sustainability reports because without the validation of a certified third party, sustainability reports can easily be exposed to greenwashing or other unethical reasons. Most interviewees relied on external parties to verify their sustainability data annually by a limited assurance process. When asked about their opinion on the audit quality of sustainability reports, interviewee 5 answered:

The auditors of the sustainability report have regulatory requirements for its quality and so far what I have seen is that the assessments are pretty consistent. The Big 4 audit firms in particular have high quality standards that they maintain and protect. (Interviewee 5)

Interviewee 2 also added:

I do not really question the quality, but I always check the scope of the verification, i.e. which indicators are included in the limited assurance process, for example is it according to the ISO 31000 or ISAE 3000 standard. (Interviewee 2)

Audit quality differences do not seem to be a concern among financial institutions which suggests that auditors maintain a key role in the sustainability reporting landscape. The Big 4 accounting firms seem to have managed to obtain reputation among the financial industry but that is not necessarily true with smaller auditors. There may be many reasons why smaller audit firms may not be valued as much, but the European Commission is making changes in the near future to the European audit market that should give smaller firms more of a foothold.

Additionally, sustainability reporting under the CSRD requirements have indirect implications on the disclosure of financial products and funds under the SFDR. The new CSRD reports will transform the way in which financial institutions have analysed ESG criteria. Interviewee 5 points out:

First of all, their internal processes (of financial institutions) will change. They've had their own ESG assessment models until now but starting in 2026 at the latest when most companies start reporting, the CSRD data will be taken better into account. I also believe that Taxonomy compliance will be the most important data that financial actors will receive. Since they have to report according to the EU Taxonomy Regulation, they can get the information from the CSRD reports. (Interviewee 5)

Financial institutions are interested in finding out if the sustainability reports will bring up any significant sustainability impacts that could affect the firm's financing possibilities. Interviewee 6 continues:

If such impacts exist, but we are still willing to finance it, we often include some kind of ESG criteria in the loan. If they are willing to make such a commitment, then the commitment to reduce emissions or other impacts becomes a shared interest. Naturally, this will also support the bank's own emissions targets, for example. (Interviewee 6)

Sustainability reports can therefore create a common sustainability goal for both parties, with mutual benefits, which also supports the green transition and is in line with EU sustainability objectives. However, it is up to the bank's risk management team to assess whether the investment has a sufficiently good risk-return ratio.

## **5.2 Sustainability in the agri-food industry**

The next section of the empirical analysis focuses on sustainability matters in the agri-food industry. As highlighted previously in section 3.3, the agri-food industry generates various environmental impacts both in the European and international context.

### 5.2.1 Relevant themes and risks

The interview questions were designed to discover which issues specific to the food industry are of most concern to the financial institutions investing in the sector. Sustainability issues related to the food industry, such as biodiversity loss, human rights issues, the circular economy, climate change and greenhouse gas emissions, were the most concerning topics. Interviewee 1 divided the main areas of interest into three points in the following way:

The first thing is that, regardless of the sector, regardless of the industry, regardless of the stakeholder group, the first thing is always carbon emissions. Always. It is the one indicator that is critically important in all countries of the planet for all stakeholders. Second, when we talk about the food industry, we are quite closely involved with nature. And now, when you think about Valio's dairy, we have dairy cattle, we have a lot of feed, and there is land use involved, so in a way biodiversity, the use of nature in general, is central and can be extended to something like the overall environmental friendliness of the production process. But then the third, and this is really important, and we get closer to the consumer. So, when the product is on the shelf, we have a buyer, so what do buyers think and value? So even if the product has been produced with poor treatment of livestock, a lot of carbon emissions, it may be that the average consumer does not care. They are interested in the price, the image, and their own well-being which leads to the fact that the product must be safe, that is the essential factor. (Interviewee 1)

The interviewee's response provides a lot of insightful information to uncover. It was made clear that financiers have a multi-dimensional approach when it comes to evaluating ESG issues in the food industry. First, carbon emissions were highlighted as one of the most crucial indicators to keep an eye on which reflects the growing recognition of climate change as a critical global issue. Second, the food industry has an intrinsic connection to natural resources. Therefore, the management of biodiversity and ecosystems is important because of the direct environmental impacts of the food industry. Third, consumer behaviour plays an important role. While environmentally friendly and ethically produced goods are crucial, consumer decisions often prioritize price, product image, and personal well-being over environmental or ethical concerns.

The agri-food industry is a resource-consuming sector where water is a vital element. This makes the sector vulnerable to climate change and also cyclical with climatic conditions. Both Interviewees 2 and 3 acknowledged that the agri-food industry strictly adheres to the ESRS standards category E. Group E of the ESRS standards refers to environmental subjects, such as climate (E1) and pollution (E2). According to the EC, the

standard E is subject to materiality which is in fact usually disclosed in the sustainability reports of agri-food companies. Interviewee 5 also noted that they strive to set zero-emission targets that are verified by a third party. Such targets must have plans in place to ensure that the target is met.

Financial market participants and financial advisors are constantly reassessing the sustainability risks associated with agri-food companies. Interviewees had differing views on what risks should be considered more important than others. Interviewee 4 believes that the stranded asset risk is the most important to consider because of its worst-case scenario.

When we talk about ESG risks, the biggest is the stranded asset risk, i.e. investing in something that has no value in the future, that is, a technology that will become worthless in the medium or long term. In the food industry there is the risk of investing in a company that produces products that will no longer be attractive to consumers in a few years' time. We have to look 5 or even 10 years ahead to see whether the product will still be appealing then and whether the company will be able to produce innovations that will be profitable 10 years from now. So, I would say that the biggest risk is when the business model is not aligned with sustainability objectives, which culminates in particular in carbon emissions and biodiversity. (Interviewee 4)

FMPs need to assess potential investments in agri-food companies not only on the grounds of current profitability, but also on whether they will be viable in the future in the light of stricter environmental regulations and changing consumer preferences. Thus, the future outlook of food products has a significant impact on the firm's future cash flows. In difficult economic periods, this is amplified when customers rely on strong product brands. Interviewee 4 emphasized the importance of aligning the company's business model with sustainability goals to mitigate risks in the long term. Companies that have the ability to innovate and adapt to future market demands also have a higher chance of succeeding.

Interviewee 6 argued that they do not have any specific ESG criteria in place for food companies although there are some so-called exclusion criteria that could disqualify a potential investment within the food industry. These criteria are often tied with environmental degradation, social injustice, or governance failures. Interviewee 6 used the following example to illustrate a practical case:

If you were to apply for funding to improve the energy efficiency of a factory in the food industry, for example, we have certain criteria, even if they are not

related to the products or production themselves. In reality, energy efficiency is what is assessed in more detail in this context and then if it were agriculture, there would be an emissions aspect and in turn would assess the sustainability of agriculture. (Interviewee 6)

It may be difficult to determine ESG risks without first knowing the specifics of the organization or project. Sustainability risks can also be challenging to identify since negative ESG consequences could go undetected in the value chain. The CSRD aims to monitor these impacts both from the inside-out and outside-in perspectives through the double materiality assessment which should take more comprehensively into account indirect emissions. It also helps allocate resources more efficiently to achieve CSRD compliance. Interviewee 3 raised some concerns about the change in consumer preferences from dairy products to oat-based products. The question here is whether dairy farms are willing to switch from milk production to oats in order to avoid diminishing demand for milk.

The EU has been supporting dairy farmers with various interventions, but it is unclear whether farmers would receive similar support for oat production. If farmers refuse to change their ways, would oats continue to be imported from other countries, such as the United States? This could have an adverse effect on the climate if more oats are being produced in the United States, which already has a different infrastructure in terms of emissions and other factors. Oats imported from outside the EU would consequently be susceptible to changes in weather conditions or manufacturing variables, which would lead to higher prices for consumers. In a competitive market, this can lead consumers to be reluctant to buy the product and move on to other brands.

### 5.2.2 Industry risk profile

Prior to investing in or financing a food company, one must familiarise themselves with the risk profile of the industry. Food safety plays a particularly important role in our society because it concerns the health of all humans. Food operators have a responsibility to protect public health and ensure the safety, quality and availability of food for all. Interviewees 1 and 2 both agree that health and safety aspects are sensitive to the food industry. Interviewee 1 recalls a scandal that painted a negative picture of the dairy industry, although it is clear that the European Union has generally stricter food regulations than the rest of the world.

Everybody still remembers the scandal in New Zealand where Fonterra was selling infant formula to China and it turned out that it had exceeding levels of some substance, so it was quite shocking news that there was something in the infant formula that should not have been there. There are supposed to be some kind of safety and health measures in place for these kinds of situations. Maybe not quite at the same level as in the medical industry, but pretty close to it. (Interviewee 1)

Scandals such as the one mentioned by Interviewee 1 have a long-lasting impact on consumer sentiment whereas in industries that are more focused in business-to-business transactions, the concerns are much more restricted. The risks can become high due to the intensive scrutiny that the sector has to endure through media and news outlets.

Biodiversity risks and human rights impacts are also higher than in other industries. Globally, the food industry is a major contributor to environmental impacts that are caused by various sources such as water and energy consumption, the use of chemicals and land use. Human rights issues are present in the value chain because agricultural and dairy productions usually require manual labour unlike in the white-collar industries. Interviewee 4 explained a net impact model called “The Upright Project” and how it is used by many firms to measure the net impact of companies’ environmental and social activities.

They do this kind of net impact measurement, where they measure the positive and negative impacts of the company's core business on the environment and society and the resources that the company uses. In a nutshell, let's say you own a tobacco company whose product is harmful and it causes cancer, so they'll measure what the tobacco company needs, what resources it needs to produce those products. It will need water, workers, environmental toxins, etc. Obviously, it's going to be a terribly negative product as a whole. If you use those same resources to produce, say, an AIDS drug, then you will clearly have a more positive product, because that product is useful to the world. (Interviewee 4)

Using the same logic as in the example but taking it further, an essential part of a food company’s longevity is to look at the bigger picture and reflect on whether the product provides a benefit to the world from a health and environmental standpoint. Projects such as Upright are beneficial to investors, businesses and policymakers because they provide innovative and scientific tools that can quantify the ESG impacts of companies. In a competitive industry such as the food industry, the Upright Project encourages companies to reassess their processes and end goals because the impacts of the value creation of companies are comparable. The net impact model of Upright provides clarity on costs

and benefits associated with a company's net impact, and also whether the company's intentions are consistent with its actions. In conclusion, the principal risks in the food industry, in addition to those associated with sustainability, include changes in consumer behaviour, regulatory changes, and challenges to the ecology and ethics of food production.

### 5.2.3 High and low-impact ESG aspects

One of the most important responsibilities of financial market participants is to be able to distinguish which are the critical factors that have a significant influence from an ESG perspective compared to the minor ones. There does not seem to be a single common factor, but FMPs prefer to utilize responsible and green bond frameworks with specific requirements for which types of projects may be financed more cheaply. Interviewee 6 elaborates:

Financial institutions have their own definition of how to categorize different projects but there may also be converging features among them. At the moment the most well-established responsible bond framework is the ICMA (International Capital Market Association) framework that follows the Green Bond Principles although lately the EU's green bond standards have also gained traction. (Interviewee 6)

ICMA's Green Bond Principles serve as a voluntary way to support issuers in defining the key components needed to issue a green bond. These principles explicitly determine the green eligibility of projects in different categories. According to Interviewee 6, the cost of the financing depends on if the target company is committed to certain objectives or criteria and on the other hand if the criteria are not met then the cost will be higher. The concept works like a stick and a carrot in a way.

The difference between high and low-impact ESG factors for larger companies is not the same as for smaller companies either. For companies with a large market share such as Valio in Finland, financial institutions need to analyse what are the most relevant ESG indicators that actually make a difference. Interviewee 1 weighs in on the matter:

In principle, the market is pretty poor if financial institutions cannot make smart judgments about what's important and what's not, according to the business model. If one of the ten indicators is showing red and therefore, they are afraid to invest in it, then they do not know how to think about it relatively from a business perspectives and how important part of the business is the one of these ten indicators. We have seen numerous examples of this, where

in practice, poor decisions are made to not invest when they are not able to identify what is essential and what is not. To some extent, it comes to the point where 700 different things are reported, which shows that the market does not know what is important and what is not important. (Interviewee 1)

Consequently, it is imperative for investors to understand both the market and the business model before making judgments about a company's sustainability. The more international the investor, the more challenging it is to make a judgment at the local level. Therefore, international institutional investors have developed a model that they follow, and they hope that it will be effective in all countries equally well. So, the undergoing criticism of the scope of reporting returns to the fact that when everything must be reported, even a minor negative indicator can make it appear worse than it actually is.

On the other hand, it is important to acknowledge the influence of large companies. Interviewee 1 added the following:

Valio as a large company helps in that if the major pieces are in place, you have to remember that banks are looking to do business. They do not want to leave Valio unfunded or not invest in it just because there is some sort of indicator there. So yes, I would say that all sorts of things will still go through the screening process, as long as there is not a clear risk. (Interviewee 1)

Institutional investors seem to be more flexible when it comes to larger enterprises compared to smaller ones. Firms that have yet to prove that they can be viewed as a legitimate player in the food industry may find it more difficult to seek financing. At the end of the day, it is all about an attractive risk-return ratio that also contributes to environmental, societal and governance factors.

#### 5.2.4 ESG analysis teams

Interviewees were asked about the activities of their ESG analysis teams to gain a better understanding of the process that financial institutions follow when assessing corporate sustainability issues. ESG professionals use standardized data, benchmarks and ratings to help them compare the performance of different firms. While each ESG analysis team has its own processes, the most common sources of information, in addition to companies' own reports, appear to be Bloomberg, MSCI and Sustainalytics. The first thing that the ESG analysis teams do, is check whether the target company has identified the relevant themes in the food industry. It should also establish measures or objectives where the company is headed. The ESG analysis teams utilize the information to assess the

“mitigation strategy” in terms of how they will pursue their goals. The risk mitigation strategy is a plan for preparing for and minimizing the effects of risks faced by the business. Interviewee 2 believes that one must take the company’s proclaimed plan with some scepticism:

It may not be very credible if a company comes up with an existing report that states a 50% decrease in emissions, for instance, but then says nothing about how it will be achieved or how the target has been reached, so these things are reviewed on a thematic basis. Obviously, it is not as easy to set targets for all themes as for others. A good example is climate change, for which there is a CO<sub>2</sub> equivalent, and biodiversity, where it is still a bit of a work in progress as to what the indicator should be. (Interviewee 2)

ESG analysis teams value clear and realistic strategies that concretize the methods to achieve the objectives set. There are still ambiguities when quantifying sustainability themes in reports. Some areas such as climate change have well-established metrics (e.g. CO<sub>2</sub> equivalents) which makes setting and measuring targets relatively straightforward. However, other areas, such as biodiversity, still lack clear and universally accepted indicators, making it challenging to assess and compare performance across companies and industries. The process of developing effective indicators for certain ESG themes is ongoing. As understanding and technology evolve, so do the metrics and strategies for assessing and mitigating impacts in areas like biodiversity.

Sustainability reports such as Valio’s are subject to the CSRD standards although typically they are regularly monitored. Often, the whole company portfolio is reviewed through the databases of the ESG analysis teams automatically on a daily basis. If deviations occur, they are monitored and the cause is investigated. Interviewee 4 explains a common procedure when this happens:

Often, investment policymakers determine the risk level of a company, and if it falls below a certain threshold, in standard practice it would require the approval of the investment manager or investment committee for further action. Then the case may be justified, for example, on the basis of expected returns or the fact that remedial measures have been taken to mitigate the risks. A more in-depth analysis is then carried out, based first on the provider's data, followed by the ESG analyst and portfolio manager conducting their own analysis. Finally, the analyses are verified to be consistent with each other. (Interviewee 4)

Practices may vary slightly from one financial institution to another, but they generally follow the same structure. Sustainability reporting is also carried out internally in

financial institutions and changes in the sustainability performance of the target company are usually detected quickly. More in-depth analyses require more work and therefore such analyses are usually reported on a quarterly basis. Reporting on corporate sustainability issues requires a lot of data analysis and risk management, which is why many financial institutions use different ESG rating systems to standardise and streamline processes.

### **5.3 ESG-based financing**

The third theme of the empirical analysis revolves around the funding of food and dairy companies. This section aims to understand what aspects are particularly important to financial institutions in the food industry and Valio. The interview questions of this section were designed to gain insights into the financial decisions of financial institutions and to identify which ESG aspects might influence them. In addition, interviewees were asked if they consider any ESG issues to be non-negotiable when it comes to financing terms.

#### **5.3.1 ESG compliance in financial analysis**

The results of the interviews suggest that the EU Taxonomy Regulation is used by financial market participants as a tool to assess ESG performance. The Taxonomy criteria generally provide guidelines for the type of credit rating a company should be given. Interviewee 5 summarised as follows:

I would think that compliance with the Taxonomy is what affects the most, that if the Taxonomy level is very low and there are no opportunities to move in a more carbon-neutral direction, then the margins will rise, which means that debt capital will be more expensive for the company. Then again, if there are good sustainable development goals and implementation methods and there is a desire to invest, and CAPEX plans are in place, then the company will probably get funding for it just fine. At the moment, the market is looking for exactly the items that can be used to increase compliance with the Taxonomy. (Interviewee 5)

Financial institutions are often willing to finance projects that may not yet have achieved Taxonomy compliance, but need evidence that progress is being made towards sustainability objectives. Setting sustainability objectives in line with the EU Taxonomy is a step in the right direction, as it covers all three aspects of ESG. In order to do that, a company's actions must qualify for the EU Taxonomy objectives. The classification

system with all its conditions can be found in the Official Journal of the European Union and on the website of the European Commission.

Interviewee 4 reflects on ESG compliance from the perspective of a venture capital investor and compares it to the financing of listed companies.

Venture capitalists may invest heavily in these kinds of turnaround companies, companies whose business model is not yet green or Taxonomy compliant, but where there is potential to make that change in the business and then create more value through ESG. It is actually a very attractive business case for an investor. In publicly listed companies, this happens less because there are so many shareholders, so the possibility of influencing is much smaller unless you buy a large stake in the company. (Interviewee 4)

There are basically two base cases when financing food companies based on ESG components. First, there is a baseline that must be met in order to invest in a business. If the level has not yet been reached, the investor needs to consider how can he or she influence the course of action of the company and what actions the company has already taken, as illustrated by the example of Interviewee 4.

Interviewees were also asked about ESG aspects that they deemed non-negotiable when discussing investments in the food industry. Interviewee 1 found it challenging for food companies that, even if a company discloses its business according to the regulations or voluntary measures, there can still occur incidents of non-compliance in its value chain. Reporting on sustainability matters does not mean that the company will not face ethical or legal challenges due to unforeseen issues in its supply chain. Interviewee 1 emphasized that despite adherence to reporting standards and regulations, there remains the potential for instances of non-compliance or unethical practices within the company's value chain that can damage its reputation and potentially affect its financial performance. Reporting is all about “stating intentions” but it does not necessarily ensure that anything is actually done about it.

Interviewee 1 believes that nowadays setting a net zero carbon emissions target is a must for any company that wants to be a part of the green transition and conduct sustainable business.

These net-zero carbon neutrality targets are certainly an issue that can be developed over time, but it has become something that is very difficult to compromise on these days, so very few companies dare to say that they are not taking net zero seriously. It is interesting in the sense that a lot of

companies had 25 years to do something about it, and today you cannot compromise on it anymore. (Interviewee 1)

Carbon emissions are directly linked to global warming and their reduction is part of the Paris Agreement to tackle climate change and its negative impacts. By setting net-zero carbon neutrality targets, companies are actively supporting the United Nation's net-zero ambitions. More importantly these commitments must also be backed by credible actions to ensure that progress is made to cut carbon emissions. Interviewee 2 shares similar thoughts as climate change and biodiversity loss should be taken more into consideration in the food industry because both will have a strong negative impact on the ability of doing business in the future. Therefore, more efforts should be made to minimize their impact. Interviewee 3 mentioned that they follow the ESRS standards set by the EC that have identified possible threats to specific sectors affecting the food industry. The double materiality analysis, which forms the basis for the EU's sustainability disclosures, has also been acknowledged as a positive change by most interviewees.

### 5.3.2 Financing trends in the food industry

There is no doubt about the rising trend of sustainability-linked finance in the food industry. This trend encourages companies to adopt more sustainable practices through loans or by tying them to ESG indicators in exchange for more favourable financing terms. Conversely, the financial sector is increasingly less willing to finance or insure certain sectors of the food industry. Especially plant-based products have gained popularity over products of animal origin, which has also increased attention on animal welfare. According to Interviewee 3, consumers are increasingly aware of food products that require a lot of water and land, such as soybeans, which reduces their demand due to the environmental impact they cause. Interviewee 4 has also noted that the surrounding political environment has a major influence on which food sectors will receive financial support over other.

Interviewees reflected mostly on the Finnish food industry where there does not seem to be any clear sector on the decline. An increase in plant-based products has been observed although it has not negatively affected the financing of meat substitutes. Interviewee 1 concluded:

Anything, involving the unethical treatment of animals is concerning, but this raises the broader question of whether eating animals is unethical. However,

I do not believe banks and insurance companies dare to take a stance on this issue, for the sole reason that it would cut off a pretty big chunk of their business. We are dealing with such philosophical questions that I doubt that we will go down that road. (Interviewee 1)

Financial institutions and insurance companies try to avoid ethical questions that could affect their reputation and business. The financing terms might be stricter for high-risk sectors but hardly any financial institutions or insurance companies are willing to refuse to finance them altogether. Interviewee 1 also anticipates that in the future there may be introduced a carbon dependent price component for all food products.

Banks and financial institutions have started to tie their loans to ESG indicators to promote sustainable business practices. Especially large-cap and some mid-cap companies such as Snellman Group, have signed sustainability-linked loans to enhance new food production and logistics capacity (Nordic Investment Bank, 2021). According to Interviewee 2 financial institutions are keen on supporting sustainable investments and initiatives that promote the companies' sustainability strategies and goals:

It is sensible to me that the role of the financier is also emphasised here, given that companies have developed effective sustainability strategies and targets, so we want to support them in achieving these goals. Naturally, we will assess whether we think they are good objectives before including them in the loan arrangements. This is a common practice in the current business environment. (Interviewee 2)

The entry into force of the Corporate Sustainability Reporting Directive means that even smaller companies will have to rethink their strategies. It will be interesting to see whether this will increase the demand for sustainability-linked loans for smaller companies. Interviewee 2 states that climate-related indicators are the most used, mainly due to the fact that the most advanced measurement mechanisms are related to climate emissions.

We have market data, though I can't recall the exact percentages right now. Most metrics are definitely climate-related because measurement and comparability are the most advanced in this area. The underlying theme throughout the evaluation process is the materiality of the themes, starting from the analysis and reporting stage and extending to the financial indicators, which must also be material to the company. (Interviewee 2)

Nevertheless, the main idea when assessing the firm's overall sustainability indicators is the materiality of the sustainability themes. The sustainability themes to which a company is committed should be consistent not only with the company's reports but also with its financial data.

Interviewee 4 has not encountered many sustainability-linked bonds in the Finnish food industry except for promising startups such as Solar Foods which are newcomers in the industry. Despite this, Interviewee 4 remains optimistic about the future:

I would imagine there are some and it would be good to have such bonds. After all, this is a huge opportunity for Finnish companies to take a leap towards sustainability, so hopefully we will see more and more of them in the future. (Interviewee 4)

Interviewee 5 believes that there is a growing interest in releasing green bonds on the market. The funding for these types of loans is not necessarily available directly from banks, but rather from the capital markets through these financial instruments.

### 5.3.3 Financier's short-, medium- and long-term objectives for the food industry

The food industry has no choice but to adapt to the changing environment of the food industry. Climate change is causing unpredictable and unfavourable climate conditions for agriculture and the dairy industry which forces agri-food companies to find innovative ways of production to meet the growing demands of the consumers. Societal and cultural views are also changing and consumers are shifting from traditional meat and dairy products to plant-based alternatives which can be seen in the diminishing number of dairy farms around Europe. Interviewee 3 believes that the upcoming sustainability reports that will be disclosed according to the CSRD will dictate the materiality of food companies' impacts.

I would expect these targets to come from the reporting results. Because these are the things that companies really have to invest in through the double materiality requirement. I also think that companies need to carefully consider through their ESRS standards what they deem to be important to them through materiality. (Interviewee 3)

The first CSRD reports that are expected to be published next year will provide better insights into sustainability issues in the food industry which will be reflected by financial institutions. There has also been discussion about the usefulness of double materiality, and whether it will only benefit the financial institutions for their disclosure requirements or will it also be beneficial for the surrounding society.

Interviewee 4 sees a lot of potential for investors as the food industry is still a long way from having established sustainable processes:

It's a defensive industry in the sense that people have to eat and so on, so in that sense it's certainly interesting to many people. The goals that are typically there are related to carbon neutrality goals, so if you look at investors' and financiers' own goals, they typically tend to be carbon neutral in 2040 and these sorts of goals. These targets are then directly reflected in the portfolio companies regardless of what the industry is, so yes, the number one goal is to reduce carbon emissions in any company, but especially in the food company. They have enormous potential, after all, food is a huge source of emissions. If you look at the individual consumer, it is one of the biggest sources. There is huge potential for emission reductions here, and that is of course of interest to financiers precisely because they are under great pressure to make their own portfolios carbon neutral. They also have to report to their own investors in compliance with the SFDR, so of course they will choose targets that support their own objectives. (Interviewee 4)

The answer from Interviewee 4 raises several points about the direction in which the food industry could be heading. It is possible that the food industry may be facing a disruption in finding solutions to reduce emissions in order to meet sustainability goals and consumer demands. The EU's 2040 greenhouse gas emission reduction target seems a realistic goal for many companies, as they have been implementing it in their sustainability strategies.

Interviewees 1 and 2 argue that they do not really set any specific sector-wide objectives but rather want to be involved in the transition to more sustainable practices. From a company's point of view, it is important to be prepared for CSRD in order to report at the level companies are expected to. Interviewee 1 reflects on this as follows:

In the short term, the goal is just to get the hang of all the new reporting requirements, all the new data needs and so on. Let's make sure that we at least keep up with it so that we don't miss what comes from the EU or from somewhere else. Getting the data right, so knowing what's being funded. There is still an awful lot of work to be done to find out what information is needed. And now, in the medium term, it will start to have an impact on the application of that information. In other words, we are now beginning to identify the places where we come from, where we are, where there is good and where there is bad, and we want to start cutting out the bad. The fact that what is bad is carbon emissions is one thing, but in the food industry there are many other things that go into the bad category that we want to try to get rid of in the medium term. In the long term, the desire is that there is no longer any kind of bad stuff in the portfolio, that is, there is a fully "Net Zero aligned" financing portfolio and can then help their own customers to get on that path and enable it to finance them. Banks want not only to finance good cases, but they want to be facilitators of this transformation. So, I think that the banks are proactive in telling us what conditions we can finance and then contribute to driving the change, so they want to be facilitators. (Interviewee 1)

Financial institutions are working to facilitate companies that are willing to transition away from fossil fuels and develop renewable energy sources. A key element for financial market participants is that they can take credit for the green transition by providing the necessary financing. Interviewee 2 also expects more cooperation with businesses with the coming changes:

The most important thing in all of this is that we want to be involved in helping to shift towards sustainability and also to be openly involved with companies in thinking about the new possibilities, because there are still not always answers to these questions. These are completely new problems that we all have to think about and, as I went through at the beginning, how our actual sustainability impacts come from our customers' business. It's not as much about our own business - email goes out, money circulates out of the account – the impacts are not as big, in a way. Our focus is on developing these things with the companies and then supporting them through our sustainable financing solutions, and when we identify good targets there, we are happy to get involved. (Interviewee 2)

Interviewee 2 desire to cooperate underlines the importance of working with food companies to achieve common sustainability goals and to address emerging challenges. The focus of financial institutions on food companies indicates that they can be strategic investment targets to satisfy sustainability commitments arising from the SFDR. It remains to be seen whether food companies' sustainability programs will meet the return expectations of financial institutions and their emission targets.

## **6 DISCUSSION AND EVALUATION OF THE STUDY**

The main contribution of this paper was to assess the multifaceted implications of ESG reporting on the investment decisions of financial institutions in the food industry. This case study is set out as an assignment for the dairy and food company Valio to particularly address the upcoming regulatory changes in the European Union concerning the Corporate Social Responsibility Directive (CSRD) and its impact on the Sustainable Finance Disclosure Regulation (SFDR). The changes in the EU's sustainability regulations will impact Valio's sustainability disclosure processes as well as many other food companies in Finland. Thus, the findings of this study are highly relevant not only to ESG professionals but also to companies and financial institutions preparing to address these changes. This thesis is also a continuation of earlier studies on sustainability reporting that have analysed the previous Non-Financial Reporting Directive (NFRD).

In this section, the empirical findings from section five will be analysed in conjunction with the theoretical findings in section three. The terminology analysis from section two also plays a role in drawing conclusions. Moreover, section 6.2 highlights managerial implications that are relevant for the future application of the new reporting requirements. Section 6.3 presents an evaluation of the study, which examines the validity and reliability or trustworthiness and credibility of the case study. As part of scientific evaluation, the generalisability and transferability of the results are also evaluated. Following the evaluation come the limitations and future research suggestions to build on. Finally, in section seven the summary outlines the main points of the study, the results and the conclusions.

### **6.1 Discussion of the results**

The study's theoretical section provided a solid foundation for the empirical results to rely on. Section 2 offered a unique sustainability reporting framework that not only classified various sustainability reporting abbreviations but also described the concepts of CSRD and SFDR which were the main topics in the results section. The ESG legislation in the EU forms part of the broader package called the European Green Deal. It is a set of policies aiming to reach climate neutrality in the EU by 2050. The EU has launched several initiatives in order to reach the ambitions set in the Green Deal and the upcoming changes in sustainability disclosure regulations support them.

For companies, the CSRD will gradually target different-sized enterprises mainly based on the size of turnover, employees and balance sheet. The CSRD will have a major impact on sustainability reporting, affecting previously established regulations such as the Transparency Directive 2004/109/EC, the Audit Directive 2006/43/EC and the Accounting Directive 2013/34/EU. The real implications of the CSRD are still unknown since firms will start to publish CSRD-aligned reports starting from 2025 onwards. This has not prevented researchers and financial market participants from proposing hypotheses and estimations about the possible effects of CSRD. Prior research on the NFRD supported the evidence that CSRD holds an integral part in recognizing sustainability as an important aspect of a company's financial valuation. This argument was further confirmed by the empirical evidence in this study that financial institutions will consider CSRD reports as a legitimate component of their financial decisions. Consequently, the expectation that due diligence processes will change in response to the updated reporting requirements is validated.

The European Commission has assigned the EFRAG to develop and finalize the European Sustainability Reporting Standards (ESRS) which are at the heart of the CSRD's requirements. The ESRS have received extensive feedback from stakeholders in the drafting and finalization phases which are both crucial steps to ensure the practical, comprehensive implementation of the standards while also being aligned to other international standards. In addition, the CSRD will enhance the quality of information by mandating that independent assurance service providers deliver an opinion based on a limited assurance engagement. It is important to acknowledge the added value brought by the increased assurance requirements under the CSRD, as companies that previously sought voluntary assurance were reporting at varying levels and on different aspects, leading to low comparability. Thus, the limited assurance engagement will not only enhance the comparability of sustainability reports but also improve the overall quality of sustainability reporting.

The empirical results show that the CSRD will drastically increase the amount of sustainability information in the market. Critical analysis of what aspects and indicators are relevant for each industry and firm will be important in order for investors to take advantage of the sustainability disclosures. Along with the CSRD, the European Commission has put forward the ESRS which are also aligned with the requirements of the SFDR. The key aspects for nearly every sustainability standard or recommendation

are the degree of alignment with other frameworks, the comparability, the transparency, the integration with financial reporting and the consistency of reporting frameworks. The findings suggest that the implications of the new double materiality concept in the CSRD will result in a higher amount of sustainability information. That data may include a lot of irrelevant information that may confuse financial institutions. A proactive preparation for future disclosure changes can yield a competitive advantage for financial institutions in the food sector if they are able to incorporate the new information flows into their financing decision-making and, together with financial reporting information, formulate the right financing terms.

Financial institutions will be able to disclose more transparently the sustainability impacts of their financial products according to the SFDR. This is because financial institutions use company data from their CSRD reports to assess the sustainability ratings of their financial products. That said, the SFDR remains an important pillar in the EU sustainability reporting landscape providing transparency and openness in the financial markets. Despite this, there has been a lot of criticism of the SFDR for its loose classification system of financial products. The lack of standardisation has caused issues for investors who are interested in comparing different investment targets. Among ESG indicators, financial institutions tend to favour climate-related metrics due to their reliability and relevance to most if not every food company. These issues among others have been noted by the European Commission which has already launched two consultations with the aim of improving the regulation (European Commission, 2023b).

The theoretical foundation of the study was further developed, highlighting the stakeholder theory, the legitimacy theory and the agency theory. All three theories offered their perspectives on what are the main priorities of companies in our society. First, the stakeholder theory addresses the group of investors, regulators and other stakeholders and recognizes the power that they have over a firm's actions. The classification of these groups is necessary in order to prioritize their needs depending on to whom the company might be held accountable. The findings of the study showed similar results as to why managers use different accounting methods to deliver a particular view of the current state of the company. Greenwashing is one of the current problems that arise from sustainability reporting as most sustainability frameworks leave room for managers to cherry pick the best performing indicators in their sustainability reports. On the other hand, the green transition has raised the expectations of companies that take part in it for

investors, customers, NGOs and other stakeholders. Companies must therefore be particularly careful that their sustainability intentions and their actions are aligned.

The second theory relies heavily on the power of legitimacy in our society. The legitimacy theory suggests, for example, that firms that lack legitimacy find it challenging to receive financing. The results confirmed this as well since less established food firms usually need to seek financing through other means than from the banks. Often the limited historical performance along with limited resources to take on sustainable projects are factors that affect the availability and terms of financing. According to the legitimacy theory, ESG reporting can serve as a means to bolster a firm's legitimacy and social reputation while justifying its sustainable development strategies. ESG professionals from financial institutions also expect such disclosures in their corporate sustainability reports, which in particular, measure the materiality of impacts and the progress towards enhanced sustainability. Active monitoring of these reports not only provides up-to-date information on the company's sustainability efforts, but also creates transparency in the relationship between the financial institution and the company.

The third theory is based on the effects of signalling information to stakeholders. According to the signalling theory, voluntary sustainability reporting can increase the awareness of SDGs and have a positive impact on the company's financing alternatives. ESG professionals stated that voluntary reports are also being analysed as a part of their screening process which makes them a relevant piece of information. As mentioned in the previous chapter, CSRD sustainability reports provide different signals for financial institutions to interpret in accordance with their financing strategies. The results provide evidence that supports the expectation of the study that the quality of sustainability reporting and metrics are increasingly considered in investment decisions.

Other expectations regarding the empirical section were also met. Financial institutions insisted on receiving reliable sustainability information from companies' value chains which might hold a large portion of their greenhouse gas (GHG) emissions. There were also arguments about the reliability of auditors in sustainability reports although it seems that financial institutions are not concerned about it. The European Commission has declared its intention to open up the auditing market, which will enhance the overall quality of audit reports and increase competitiveness within the European audit market. This will reflect in an increasing demand for auditors, which is also due to the

implementation of the mandatory limited assurance for companies under the scope of CSRD.

When interviewees were asked about the objectives in the food industry, it seemed that the common approach to setting sustainability objectives is through a sustainability-linked bond. Sustainability-linked bonds have financing conditions that are linked explicitly to sustainability conditions in order to incentivize the bond issuer to achieve its sustainability targets. Interviewee 1 claimed that in the short term, their objective is to be internally prepared for new disclosure processes whereas in the long term they want to be involved in the transitioning of companies from “brown” to “green” projects. Other interviewees also acknowledged identifying potential projects where they could facilitate the shift towards more ESG-friendly outcomes. Energy efficiency is seen as a key performance indicator (KPI) for financial institutions and can be used to measure the overall sustainability of a factory. Interviewee 6 mentioned that enhancing the energy efficiency of a project is often a priority for financiers and typically involves meeting specific criteria. Additionally, the European Union's agenda includes the transition to more efficient and sustainable energy use, which can serve as a compliance mechanism for financial institutions.

One of the main problems that the upcoming regulatory scrutiny is causing for food companies are the short-term compliance costs of developing robust data collection mechanisms throughout the supply chain. The double materiality assessment can cause significant challenges especially in the food industry. The monitoring of both the impacts on the outside world and the sustainability risks and opportunities involved with the organization across the supply chain might not yet be feasible. Therefore, stakeholder engagement is emphasized in order to achieve longer-term strategic gains from EU's evolving regulatory environment.

To conclude, the tightening regulatory landscape in sustainability is prompting to greater emphasis on due diligence processes and policies. The findings indicate that financial institutions are developing new valuation models that are better adjusted to the CSRD reports. Given that previous research has highlighted the low reliability and high subjectivity of sustainability data, more rigorous and holistic attention to companies' ESG aspects will expand the data points available for analysis. This approach will result in more accurate and higher-quality information to support decision-making.

## 6.2 Managerial implications

This study will improve the comprehension of market investors and financiers on social and environmental sustainability and its impact on overall firm performance, with a particular focus on food companies. Such insights can inform future assessments of firms' financial and ESG performance, guiding decisions on whether to apply premiums or discounts to financing terms. Consequently, financial institutions are motivated to move beyond greenwashing or altruism and to embed social and environmental sustainability into their strategic goals and business performance metrics. As financiers grow more sophisticated and better understand the future financial implications of various types of information, sustainability reports increasingly reflect this information with greater accuracy and less bias. This informational improvement in the sustainability reporting landscape suggests that opportunities based solely on informational asymmetries have decreased.

The strategic considerations from this case study are diverse. Firstly, managers, whether from a company or a financier's perspective, can use this study to stay informed about the current regulatory landscape for sustainability reporting and take appropriate actions based on their organizational needs. For Valio, the study sheds light on the perceptions and expectations that financiers have regarding the CSRD reports of food companies. The findings from the empirical section are comparable to other studies focusing on the CSRD and SFDR developments, while the focus on the food industry offers additional insights into a specific sector. Even if the food industry is not directly relevant from a managerial standpoint, there are industry-specific similarities that are applicable to other industries, such as manufacturing or energy.

Secondly, there are unrealized synergies from reporting under the CSRD and SFDR. While the CSRD creates the requirement for companies to comply with the ESRS, the SFDR uses the same data at the entity and product levels to evaluate sustainability risks and classify investments depending on how embedded sustainability aspects are in the fund. By aligning the data requirements of both directives, companies can streamline their reporting processes and reduce redundancies. Although not mandatory, such alignment allows for a more cohesive approach to sustainability reporting where the data collected for regulatory compliance also serves to inform investment decisions.

Finally, adapting to new disclosure requirements can be both time-consuming and costly, as it may involve changing corporate operations and other internal processes. To facilitate a smooth transition, it is crucial to train the staff on the new reporting standards and prepare for the added workload to maintain continuous compliance. This can be done for example by hiring external consultants or auditors that specialize in sustainability reporting to provide guidance and support. Taking proactive measures such as these can increase investor confidence who are more likely to trust and invest in companies that demonstrate transparency and a robust approach to managing sustainability risks (Clark et al., 2015). Investing in the changes required ahead of time to meet the upcoming rules will help food companies mitigate the risks of greenwashing inherent to the industry and contribute to broader societal sustainability efforts. This involves actions such as collecting sustainability data and redefining their branding and market positioning. (Toussaint et al., 2021.)

### **6.3 Evaluation of the research**

The evaluation of scientific inquiry involves examining its authenticity and integrity, as suggested by Lincoln and Guba (1985). In qualitative studies, the researcher plays a pivotal role as an instrumental part of the investigation. Hence, the integrity and robustness of the entire investigative process deserve to be scrutinized. Broadly speaking, the evaluation of research reliability encompasses three dimensions. The criteria established by Lincoln & Guba (1985) for assessing the integrity of qualitative research, building upon Guba's earlier work from 1981, serve as a foundational framework for evaluating the reliability of this study. Guba's (1981) analysis laid the groundwork by defining four essential aspects applicable to both qualitative and quantitative research methodologies. These aspects—known in the context of qualitative research as credibility, transferability, dependability, and confirmability—originate from concepts of truth value, applicability, consistency, and neutrality. This framework, further detailed in works such as Krefling (1991) and Lincoln & Guba (1985), provides a comprehensive approach to ensuring the rigor and trustworthiness of qualitative inquiries. (Guba, 1981; Krefling, 1991; Lincoln & Guba, 1985)

Firstly, credibility pertains to the alignment of the researcher's interpretations and conceptual framework with the experiences of the participants (Eskola & Suoranta,

1998). In the context of this study, credibility is enhanced through the practice of posing supplementary questions or recapitulating the responses of participants.

Secondly, transferability relates to the applicability of the study's findings to broader contexts (Lincoln & Guba, 1985). This study seeks to augment transferability by evaluating the saturation point of data collection which is also discussed in section 6.4. Nonetheless, given the relatively limited scope of case studies examined, the extendibility of these findings is inherently constrained. The aim here is to shed light on the phenomenon under observation through a select number of case studies, rather than to establish a universally applicable model.

Thirdly, to address the dependability of the study a positivist researcher must conduct the research process in a way that can be replicated in the same context, using the same methodology and with the same participants. By acting so, similar results would be obtained. However, as noted by Fidel (1993) and Marshall and Rossman (2014), the evolving nature of phenomena, such as the EU's regulatory framework in sustainability reporting, poses challenges for qualitative researchers. Florio-Ruane (1986) points out that the study's findings are closely tied to the specific case in the food industry, arguing that the results are effectively "frozen" at the time of publication. To properly address concerns about reliability, the processes of the study were reported in detail so that future researchers can repeat the work even if the results might differ. This comprehensive documentation will also allow readers to assess whether the study followed proper research practices. (Shenton, 2004)

Lastly, confirmability is concerned with the extent to which the study's findings are consistent with those of existing literature on the subject matter (Eskola & Suoranta, 1998). Efforts to bolster confirmability in this investigation include presenting its outcomes alongside those of other related studies. Given the novel nature of the research theme and the scarcity of research specifically on CSRD, this study's findings are compared with those from investigations focusing on NFRD and other related sustainability regulations.

## **6.4 Limitations and further research suggestions**

It is important to acknowledge and address several limitations that impact the research process. These limitations are primarily associated with the novelty of the new EU

directives, the limited availability of ESG metrics in the food industry, the absence of concrete Corporate Sustainability Reporting Directive (CSRD) reports, and the lack of research on the effects of the new legislation. One of the primary limitations stems from the novelty of the CSRD and SFDR policies. The information provided in this study is restricted to the timing of its publication and cannot account for developments thereafter. The Directives and their proposed changes have been introduced recently, meaning there is not sufficient historical data available to evaluate their long-term effects. Financial institutions and investors are still in the process of incorporating these new directives into their investment strategies. The scope of the research will also be exclusive to Valio Oy's relevant financing alternatives, consisting of loan financing.

Another significant limitation lies in the availability and consistency of ESG metrics in the food industry. Compared to other sectors, the food industry has fewer standardized and readily available ESG metrics which makes it challenging to analyse its effects in financing decisions. A critical issue in researching the impact of ESG reporting on investment decisions in the food industry is the absence of concrete CSRD and SFDR reports. Given the relative newness of these reports, companies and financial institutions within the industry may still be in the process of adapting to the new reporting requirements. Thus, the scarcity of research makes it challenging to establish a clear causality between ESG reporting and investment choices.

The methodology of this research raises questions about the validity of the results. In this context, the number of semi-structured interviews reached a saturation point during most interview questions, indicating that more interviews would not have added value to the findings. The advantage of a case interview is to gain internal validity to support the claim about the causes and effects of the evolving regulatory environment in sustainability. Naturally, this limits the external validity of the study meaning that may be harder to generalize the findings of this study due to subjectiveness of the results.

As a concluding remark, this study lacks the resources to conduct a broader qualitative analysis of the implications of CSRD on financial institutions. More extensive data would be needed to generalise the results. With a limited number of semi-structured interviews, this study provides a contextual understanding of the topic. At the time of carrying out this study, the first sustainability reports under the CSRD are yet to be published. Therefore, the analysis is based on the provisions of the Directive and the expectations of

financial sustainability professionals. This assumption inherently affects the practical applicability of the results of the study, given that the impacts are still to be realized.

Further research is necessary to address the developments and changes not only in the ESRS standards, but also in the sustainability reporting landscape. The European Commission is already working closely with investors, companies, NGOs and other stakeholders in order to find the best alternatives to a harmonized, transparent and useful set of standards that benefit all stakeholders. The constantly changing sustainability reporting environment and its implications for the environment and society will continue to be an important area for research. Additionally, examining changes in the demand for ESG information over time represents another important research gap. Scientific research provides policymakers with valuable insights on future trends in sustainability reporting. Notably, the food industry has been under-researched despite its significant impact on emissions.

## 7 SUMMARY

This study was motivated by the new regulative changes in the sustainability reporting framework of the EU. The recent changes in CSRD and SFDR are reshaping the way of sustainability reporting and understanding its impacts will become crucial for adapting to the evolving regulatory environment. The transition from voluntary sustainability reporting to tightening regulatory scrutiny plays a vital role in financing the green transition by promoting more transparent disclosures. Environmental, social, and governance (ESG) factors have become crucial in assessing the long-term sustainability and ethical impact of investments. Investors and financial institutions are increasingly incorporating ESG criteria into their decision-making processes to mitigate risks and capitalize on sustainable opportunities.

The study's main research question was to examine how does ESG reporting affect the investment decisions of financial institutions. The research was focused on the food and dairy company Valio's industry i.e. the food industry and it was designed to be a case study focusing on the needs of Valio, thus limiting the scope to the European agri-food industry. The aim was approached by analysing the implications of the new regulatory changes to the decision-making process of financial institutions and assessing the objectives and risks of the food industry for financiers. To complement the main research question, two additional sub-questions were proposed to identify industry-specific factors. The first one attempts to understand what kind of sustainability-related risks financial institutions consider the most relevant in the food industry and the second one seeks to find particular aspects important to financial institutions in the food industry and Valio.

For this purpose, ESG professionals working in the financial sector were approached. The data was collected through six (6) semi-structured interviews using two transcription software to minimize any misunderstandings while handling data. The data was then analysed thematically, dividing the responses into three main themes: sustainable finance and auditing, sustainability in the agri-food industry and ESG-based financing.

The study yielded several interesting findings. First of all, food security is a critical element for any society which is why food companies hold an important role in providing a reliable food source for the people. This increases the importance of their supply chains

when assessing the sustainability performance of food companies. Secondly, the main risks identified by financial institutions were carbon emissions, biodiversity loss, human rights issues and the stranded asset risk. Climate-related indicators are currently more advanced than other factors which causes bias as companies tend to tie their loans to the most reliable indicators. Thirdly, the changes in consumer behaviour can suddenly pose a risk to Valio's business which is also connected to the stranded asset risk. Strong product brands are important to ensure the long life cycle of food products. Thus, it is crucial to stay on top of the food trends and understand the cultural and societal changes that might be causing a shift in consumer behaviour. Evidence of consumer behavioural changes can be observed in the increased consumption of plant-based food products and the recent increase in investments by food companies. Lastly, financial institutions still value the risk-return factor highly in sustainability projects. They are eager to participate in the green transition of firms as long as the project is capable of demonstrating that the sustainability targets are realistically achievable such as net zero carbon emissions or energy efficiencies.

Furthermore, this study adds to the scientific literature by investigating the relatively under-researched area of mandatory sustainability reporting. The evidence supports previous findings on mandatory sustainability disclosures suggesting that they can lead to positive environmental and social outcomes, thereby facilitating more informed investment decisions. Practically, the study offers managers strategic insights to help them gain a competitive advantage in reporting sustainably. By analysing this case study, managers can better understand the implications of the CSRD and SFDR.

As the global sustainability reporting landscape evolves, it will be interesting to see whether the upcoming changes will be enough to achieve harmonisations and standardisation of global reporting standards to support investment decisions. If these changes fall short, it will be crucial to see the subsequent steps taken by regulatory bodies in the EU and globally to drive sustainable change through financing.

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## **APPENDICES**

### **Appendix 1 Interview questions**

This section presents the interview questions used for the empirical part of the study and explains the methods used to handle the data. The research question is, “How does ESG reporting affect investment decisions by financial institutions?” To answer this question effectively, real-world evidence supporting the theoretical framework is necessary. Therefore, six semi-structured interviews were conducted with various professionals who could provide their insights on the topic. The interview questions were designed to address all three research questions, which were categorized into three themes: SFDR reporting requirements, sustainability, and funding. All questions were framed from a financier’s perspective, aiming to understand their views on how food companies should comply with CSRD requirements.

Follow-up questions were asked to some interviewees depending on the need to expand the quality of an answer. For instance, in the second question, some interviewees were asked whether any criteria were set for the auditor of the sustainability report. Other follow-up questions referred to qualitative requirements and differences of auditors. In the eighth question, a follow-up question was used to delve deeper into whether ESG analysis teams utilize different tools for assessing the food industry compared to other sectors. During the ninth question, a few interviewees were asked about potential thresholds for the results of ESG evaluations and whether they place more emphasis on a specific ESG topic.

RESEARCH QUESTIONS	THEME	INTERVIEW QUESTIONS
How ESG reporting affect investment decisions made by financial institutions especially in the food industry?	SFDR reporting requirements	1. How will CSRD reporting by (food industry) companies affect your assessment process for these companies? 2. Do you assess the audit quality of a sustainability report? Why? 3. How does the ESG reporting of companies for CSRD impact the due diligence process when considering investments in the food industry?
What kind of sustainability-related risks financial institutions consider the most relevant in the food industry?	Sustainability	4. Which topics are particularly important for financiers in relation to the food industry and Valio's dairy and food sector? 5. What sustainability-related risks are given priority when assessing food industry companies for investment, and how are these risks quantified? 6. How does the risk profile of the food industry differ from that of other sectors regarding ESG concerns? 7. How do financial institutions differentiate between high- and low-impact ESG aspects when evaluating companies like Valio? 8. How does the ESG analysis team of financiers' work (what sources are used for the analysis, how is the company's performance assessed, how often is the level monitored, etc.)?
What aspects are particularly important to financial institutions in the food industry and Valio?	Funding	9. How does the results of the ESG evaluation affect the financing of food/dairy companies? 10. Are there any ESG aspects that are considered non-negotiable versus those that can be developed over time? What about in the food industry? 11. Are there any areas of the food industry where funding or insurance may be on the decline? (cf. fur farming) 12. To what extent has the food industry tied its loans to ESG indicators? Or planning to do so in the coming years? 13. What are the financiers' short-, medium- and long-term objectives for food industry operators?

## **Appendix 2 Data management plan**

The empirical data for the study will be collected through interviews with volunteers, recorded on the Microsoft Teams video recording service. Permission to use the data has been obtained from the interviewees in accordance with the objectives of this thesis. According to Article 6 of the EU General Data Protection Regulation, the processing of personal data is necessary for scientific research purposes and is based on the mission of the university as set out in Article 2 of the University Act (558/2007) and its performance in the public interest. During the interview gender, job description and experience and current job title will be collected for data management purposes. Interview recordings have been transcribed and compiled into a text file while direct identification information has been removed.

After recording, the research data will be stored on the Seafile server, a cloud storage service operated by the University of Turku. The cloud servers are owned by the university, so the data stored on Seafile will not be passed on to third parties. The maximum retention period for the research data is five years from the date of approval of the thesis. After this period, the data will be securely destroyed.