

*MARCELLIN M. YOVOGAN*

## **FIRM PERFORMANCE AND NON-FINANCIAL REPORTING IN BULGARIAN COMPANIES**

### **Introduction**

The valuation of firm performance has always been critical for business success in addition to its use by potential and actual investors, financial analysts, scholars.

Financial performance indicators have dominated the traditional approach of performance valuation. Many non-financial metrics are widely used to enhance the sustainability perspective of firms. Although, Bulgarian companies have discovered at a late stage about the benefits of, market-based management, an increasing number of them are making an effort to comply with non-financial reporting standards and guidelines. The purpose of this article is to highlight non financial performance indicators as disclosed by Bulgarian companies. It is an attempt to study the extent of non-financial reporting by Bulgarian companies. The data was collected from financial statements, management reports and publications in various company websites, the Bulgarian stock exchange, the Trade register and reports from the United Nations and other international organizations.

### **Performance measurements: From EVA<sup>TM</sup> (Economic Value added) to social responsibility**

The limitations and dysfunctional actions associated with using a ratio to evaluate firm performance have been known and discussed for decades. The economic value added concept has been developed by the Stern Stewart consulting organization to overcome traditional financial metrics. It extended the classical residual income measure by deriving the cost of capital based on the industry and risk characteristics of individual divisions. EVA is also calculated after adjusting for distortions introduced by generally accepted accounting principles required for financial reporting. EVA is proposed as an internal measure that takes into account the factors that build a premium or a discount into the market value of a company (Stewart, 1991).

The EVA method is suggested to be one of the best forms of firm financial performance measurements. The current discourse assumes that managing for shareholder value and managing for stakeholder value is different.

Kaplan and Norton (1992, 1996) argued that companies should consider four perspectives that drive firm performance in the balanced scorecard:

- Financial – How should we appear to our shareholders?
- Customer – How should we appear to our customers?
- Internal business process – Which business processes must we develop to satisfy customers and shareholders?
- Learning and growth – How will we sustain our ability to change and improve in order to achieve our vision?

The balanced scorecard integrates non-financial indicators in group of factors that drive firm performance (Kaplan & Norton 2001). In this aspect, the valuation of firm performance should take into account various aspects of business organizations and environment, which impact the sustainability of the firm. Presently, non-financial performance indicators are primarily reported by Bulgarian firms in order to comply with professional or international bodies and guidelines.

### **Non-Financial measurement and Sustainability Reporting in Bulgarian Companies**

A substantial amount of research has been covered in recent years in understanding the nature and motives for corporate social responsibility (Anderson, 1989; Arlow & Gannon, 1982; Carroll, 1979; Clarkson, 1995; Mc Williams & Siegel, 2001; Pava & Krausz, 1996; Waddock & Graves, 1997; Wood, 1991). In the same line, the role placed on corporate social responsibility by investors, analysts, managers and academics has consequently grown in many parts of the world. Business and government interest towards corporate social responsibility issues in Bulgaria has increased considerably during the last decade. However, very few studies about the current state of sustainability reporting in Bulgaria have been publicized so far. Still, there are some surveys covering a broad range of corporate social responsibility practices in Bulgaria.

The Economic Policy Institute has also published relevant research – Reporting on Corporate Social Responsibility (CSR) by the Forty Largest Listed Companies in Bulgaria<sup>1</sup>, which analyzes company disclosures in three specific areas – Corporate Governance; Environmental Policy and Social Policy during the period from March 2007 to June 2007. The enterprises surveyed are listed as the largest top 40 companies on the Bulgarian Stock Exchange – Sofia according to their market capitalization as of March 1, 2007 (accounting for approximately 83% of the total market capitalization on the BSE-Sofia).

The research showed that the majority of the companies publish more information about corporate governance issues on their websites than in their annual reports. The most commonly disclosed component by the listed entities (55%) was their corporate governance structure.

---

<sup>1</sup> Economic Policy Institute, “Reporting on Corporate Social Responsibility (CSR) by the Forty Largest Listed Companies In Bulgaria”, Sofia 2007.

Concerning the status of reporting on environmental policy, the survey revealed that only 17.5% of the surveyed companies stated on their websites whether they complied with industry-specific, national and/or international regulations regarding environmental standards. Only 10% of the companies disclosed the names of individuals or the department responsible for environmental management and compliance. These companies did report on their environmental performance, including efficient use of resources, emissions and waste on their websites (companies reporting on energy and water use – 2.5%). In comparison, the annual reports presented less data; between 0 and 5%.

The picture of social reporting is similar to that of the Environmental Policy reporting, thus 15% of the top 40 listed companies disclosed information about their community sponsorship programs on their website, followed by the disclosure of environmental policy and employee development or employee benefit policies with respectively 12.5% and 10%. The least information available was about the companies' health and safety policy (2.5%). Regarding the disclosure in their annual reports, employee development, employee benefits and employment policies are the most widely reported Social Policy issues among the surveyed enterprises (7.5–15%).

The conclusion that can be drawn from the Economic Policy Institute study (2007) is that the companies surveyed disclose more information on corporate governance than on environmental and social policy. This could be partially explained by the companies' familiarity with the corporate governance principles and the many initiatives conducted in the field. As a result of all of these, Bulgarian business seems to better understand the necessity of corporate governance disclosures.

A research report on Corporate Social Responsibility (CSR) in Bulgaria<sup>2</sup>, carried out by Alpha Research Agency for the period March-May 2007, revealed that, no Bulgarian companies use generally accepted formal methods of disclosing publicly their activities related to corporate social responsibility, as in the GRI guidelines. The survey also showed that as a whole, companies limit themselves to publishing short financial statements which do not contain details about their corporate social responsibility practices, even where the latter exists. The local subsidiaries of multinational companies do not have a separate Bulgarian report on social responsibility, but refer to the global sustainability reports prepared by their parent companies. Thus, companies have made the strategic decision to maintain an image of a large global company. Another finding of the study concerning the way Bulgarian companies demonstrate their business transparency and accountability is that the most "popular form of reporting social initiatives is in the News section of their websites". The survey also mentions the *Communication in Progress* as "one of the main voluntary responsibilities of the member companies of the Global Compact", but states that "Nevertheless, interest in reporting, as well as its practice, is still limited."

---

<sup>2</sup> United Nations Development Programme, Country Office Bulgaria, 2007 "Corporate Social Responsibility in Bulgaria – the New Challenges 2007".

### Non-financial information disclosure of Bulgarian companies

Four groups of companies in four selected industries have been studied. The choice of companies is based on their size defined as the total revenue over total assets and industries. To avoid similarity, both listed and not listed companies on the Bulgarian stock exchange have been included in the sample of study. The groups are summarized in table 1. For simplicity the companies are classified in the four industries as: company A, company B, company C and company D.

The four industries are representative, so as to draw conclusions on the ability of Bulgarian companies to disclose non-financial information. A large number of companies would have been included in the research as had been done by C. Albert and T. Günther (2010) in their study of STOXX Europe 600 firms.

Table 1

Group of companies included in the research

Company – group	Industry	Ranking – Total operating revenue/ Assets	Accountability/ ranking 2008
A – non listed	Energy	4	1
B – listed	Pharmaceuticals	5	18
C – listed	Telecommunications	2	13
D – listed	Banking	2	3

In order to compare companies' non-financial reporting, the Global Reporting Index (GRI) was used. The comparison was made against the following 11 standard disclosures according to the GR. Index.

Table 2

Standard disclosures

GRI-G3 – Standards		Abbreviations
1	Strategy and Analysis	SA
2	Organizational Profile	OP
3	Report Parameters	RP
4	Governance, Commitments, and Engagement	GCE
5	Management Approach	MA
6	Economic	EC
7	Environmental	EN
8	Social: Labor Practices and Decent Work	LA
9	Social: Human Rights	HR
10	Social: Society	SO
11	Social: Product Responsibility	PR

### Financial and non-financial reporting within industries

It can be seen, that ROE (Return on equity) of the studied companies has been relatively high for both periods of the research. A longitudinal analysis would give a deeper insight to any relationship of non-financial reporting and financial performance in Bulgarian companies. The focus seems to be merely on financial performance, rather than sustainability performance, which is evidenced by future development goals disclosed in their annual reports.

Table 3

Financial performance indicators of studied companies

Financial performance metrics	Energy		Pharmacy		Telecommunication	
	2009	2008	2009	2008	2008	2009
Current ratio	0,39	0,58	1,37	1,68	0,79	0,93
Quick	0,37	0,56	0,9	0,9	0,74	0,80
Net Profit margin, %	1,98	1,44	17,64	11,34	7,72	3,57
Assets turnover	2,44	2,85	0,47	0,45	0,55	0,53
EPS	NA	NA	0,25	0,15	0,28	0,13
ROE, %	23,79	24,49	13,27	8,94	20,36	5,43
ROA, %	4,84	4,11	8,27	5,10	4,26	1,88
Debt-to equity	3,41	4,30	0,60	0,76	3,84	1,90
Debt-to-total assets	0,69	0,72	0,37	0,43	0,79	0,65

### The energy industry – company A

Energy utilities is an industry sector having huge economic, environmental and social impacts, which implies that big companies such as the ones selected should have comprehensive corporate responsibility reporting in order to respond to the interests of the various stakeholders. The only “strong” reporting area of company A is “Organizational Profile” (100%), followed by “Strategy and Analysis” (50%). These two groups of non-financial disclosures should constitute only the preamble of sustainability reporting as they include primarily general information about the company and its attitude to corporate social responsibility (sustainability).

Despite the enormous effect of the gas distributors on the environment, the “EN” disclosure section of company A is the least touched reporting area (only 10% of the GRI Indicators were disclosed). However, the company was proactive in several environmental issues in 2009, such as greenhouse emissions, environmental initiatives and membership in green organizations.

As far as social disclosures are concerned, it should be noted that 6 out of the 10 UN Principles are related to human rights and this seems to be the reason why the Bulgarian participant in Global Compact has established a basis for reporting social issues, such as training and education, health and safety, and human rights policies.

As a whole, company A has covered in its annual reports the minimum number of sustainability disclosures.

### **The pharmaceutical Industry – company B**

The healthcare sector is characterized by constant scrutiny in respect to the way it operates by engaging a wide range of stakeholders due to its paramount impact on human life. Media coverage of the industry's activities has often been negative, which suggests that pharmaceutical companies should pay greater attention to their public image and openly demonstrate their social responsibility. Critical sector-specific (CSR) issues are clinical trials, drug safety and promotion, access to medicines, protection of intellectual property, workplace health, safety and environment. Also, the adverse environmental impact of pharmaceutical producers, such as chemical pollutants and waste disposal should not be neglected.

As far as the non-financial disclosures are concerned, it can be maintained that the level of CSR reporting is far below what should be expected from the pharmaceutical manufacturers in Bulgaria. The company has a reasonably introduced profile, overall strategy, risk assessment and management approach in its annual report, however, it has only touched basic economic, social and environmental issues in the UN COP. Disclosures about human rights were limited mainly to non-smoking initiatives, and non-discrimination policies. Environmental initiatives, expenditures and membership in eco-organizations were also covered.

The limits in non-financial reporting of this group are the lack of quantitative data (non-financial performance indicators) illustrating the outcomes of CSR policies, poor structure of CSR information in annual reports, and little information about stakeholder engagement practices.

### **The telecommunication industry – company C**

Telecommunications is a high-tech industry sector with significant economic and environmental impacts. However, the biggest effect that telecom operations have is on society. Key industry-specific sustainability issues which should be addressed by the companies in the sector include: possible adverse effects of radio waves/electromagnetic field emissions on human health, access to telecommunication products and services in remote/rural areas, security and data privacy, carbon footprint, energy and water consumption, product lifecycle management (disposal & recycling). In contrast to many telecommunication companies in Europe, company C has not yet incorporated sustainability issues in their annual reports.

The only GRI disclosures made in the 2009 annual report relates to profile, risk assessment, corporate governance and key financial figures. No separate CSR reports had been issued. However, the poor level of sustainability reporting does not mean that corporate social responsibility is not integrated in strategy and operations. Social policies and initiatives carried out have been disclosed through websites.

### The banking industry – Company D

It should be noted that the banking industry is the first financial services organization in Bulgaria to issue a CSR report by applying the GRI guidelines. It indicates its dedication to sustainability issues and commitment to continuous improvement. Nevertheless, the fact that it did not publish a CSR report in 2009, casts doubt as to whether it will carry on and develop non-financial reporting practices in the future.

What distinguishes the bank's sustainability reports from the other industry CSR disclosures is their post-financial crisis response. Being key players during the financial crisis, banks now have the urgent task to provide clear communication on the implemented measures to prevent another collapse of financial markets. Hence, specific nonfinancial disclosures of the banking industry include: restoration of trust, compensations of executives, professional expertise, responsible lending, risk management, and the future form of the international regulatory framework.

As far as the Bulgarian banking industry is concerned, it can be affirmed that the post-crisis response is not that extensively covered in CSR reports. Nevertheless, it has reported on most of the GRI indicators, including risk management, effects of the crisis on the bank business and its employees, dedication to transparency and open communication. It has achieved prominent coverage on economic and labour practice disclosures, which gives it the potential to become a model for sustainability reporting in Bulgaria.

Table 4

Financial performance and GRI reporting in the banking industry

Performance metrics	2008	2009
Current ratio	NA	NA
Quick	NA	NA
Net Profit margin	46,37%	29,28%
Assets turnover	0,07	0,07
ROE	21,82%	12,15%
ROA	3,10%	1,96%
Debt-to equity	6,03	5,21
Debt-to-total assets	0,86	0,84

Because of the particularities of the banking industries some indicators have not been calculated.

At this stage of the research, any influence on the non-financial reporting and performance indicators calculated cannot be derived. This in fact was not the objective of the study. Further research will focus on the impact of non-financial disclosure and Bulgarian companies.

## Conclusion

This study confirms that, the number of Bulgarian companies disclosing non-financial information has been increasing. For example, if 10 years ago, companies had respected the generally accepted accounting principles and national accounting standards, it could be said that most of them are publishing information, which is not necessary financially.

For performance valuation of Bulgarian companies, it would be ideal to integrate at some extent the combined use of financial and non-financial information in their reported statements. It is important to notice, that non-financial disclosure depends on the size of the company, the industry, and if it is listed on the stock change.

No specific relationships were established between non-financial disclosure and financial performance.

Further research will focus on the relationships between non-financial reporting and the overall performance in Bulgarian companies.

## References

- Albert C., Günther: *Disclose or not disclose: determinants of social reporting for STOXX Europe 600 firms*, "Journal of Management Control" December 2010, Vol. 20.
- Anderson J.W.: *Corporate Social Responsibility*, Greenwood Press, Connecticut 1989.
- Arlow P., Gannon M.J.: *Social Responsiveness, Corporate Structure and Economic Performance*, Academy of Management Review, issue 7, 1982, pp. 235–241.
- Berthelot S., Cormier D., Magnan M.: *Environmental Disclosure Research: Review and Synthesis*, "Journal of Accounting Literature" 2003, 22: 1–44.
- Carroll A.: *A three dimensional model of corporate performance*, "Academy of Management Review" 1979, no. 4, pp. 99–120.
- Clarkson M.: *A stakeholder framework for analysing and evaluating corporate social performance*, "Academy of Management Review" 1995, vol. 20, iss. 1, pp. 92–117.
- Economic Policy Institute, "Reporting on Corporate Social Responsibility (CSR) by the 40 Largest Listed Companies in Bulgaria", Sofia 2007.
- GRI, "The Transparent Economy – Six tigers stalk the global recovery – and how to tame them", 2010.
- Kaplan R., Norton D.: *The balanced scorecard: measures that drive performance*, Harvard Business Review, January–February 1992.



- Kaplan R., Norton D.: *Using the balanced scorecard as a strategic management system*, Harvard Business Review, January–February 1996.
- Kaplan R., Norton D.: *Transforming the balanced scorecard, from performance measurement to strategic management*, March 2001, Accounting Horizon, Vol. 15, No. 1.
- KPMG. International Survey of Corporate Responsibility Reporting 2008. Amsterdam.
- McWilliams A., Siegel D.: *Corporate Social Responsibility: a theory of the firm perspective*, Academy of Management Review, issue 26, 2001, volume 1, pp. 117–127.
- Pava M.L., Krausz J.: *The Association between Corporate Social Responsibility and Financial Performance: The Paradox of Social Cost*, Journal of Business Ethics, Issue 15, Volume 3, pp. 321–357, 1996.
- Stern J., Stewart G.B., Chew D.: *The EVATM: Financial Management System*. Journal of Applied Corporate Finance 8:2, 32–46. Journal publisher Stern Stewart Management Services Inc., 1995.
- Stewart III, G. B. EVATM: fact or fantasy. Journal of Applied Corporate Finance 7, Journal publisher Stern Stewart Management Services Inc. (Summer, 1994), 71–84.
- Waddock S., Graves S.: *The corporate social performance – financial performance link*, Strategic Management Journal, no. 18, pp. 303–319, 1997.
- Wood D.J.: *Corporate social performance revisited*, Academy of Management Review, vol. 16, iss. 4, pp. 691–719, 1991.

*Dr Marcellin M. Yovogan*  
*Sofia University “Kliment Ohridki”*  
*Faculty of Economics and Business Administration*  
*Department of Finance and Accounting*

### **Summary**

Firm performance is widely measured through the use of financial indicators, such as ROI, ROA or EVA<sup>TM</sup>. This article aims at highlighting non financial performance indicators as disclosed by Bulgarian companies. We studied the financial statements and management reports of a sample of companies from different industries, in order to find, to which extent, non-financial information disclosure was available. Social responsibility, human capital and environment are key non-financial indicators studied and based on the Global Reporting Index (GRI) guidelines. We found, that the financial services industry tends to publish sufficient non-financial performance indicators, and has been spearheading the adoption of non-financial information disclosure guidelines. Companies listed on the Bulgarian stock exchange, tend to report more non-financial information than non-listed companies. Large-scale firms disclose more non-financial information than SMEs. Finally, no relationship between non-financial reporting and firm performance was established, though the firms studied showed positive financial indicators. Non-financial reporting is used for communication purposes rather than for perspectives on performance valuation.

