

Master in Management FINANCIAL AND ESG REPORTING

Fall, 2024



**Lisbon School
of Economics
& Management**
Universidade de Lisboa

Faculty Team

Rita Fuentes Henriques (coordinator)

Yi Wang

My contacts



Yi Wang



Invited Assistant Professor



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Office 303, Miguel Lupi



Office hour: 14:15-15:15 on Tuesday

Who am I?

PhD in Accounting, Durham University, UK (2020-2024)

Teaching:

- Introduction to Financial Accounting (undergraduate)
- Financial Accounting and Reporting (postgraduate)
- Auditing and Accountability (postgraduate)
- Modern Accounting Research (postgraduate)

Research Interests:

- Corporate Reporting
- Corporate Social Responsibility Disclosure
- Corporate Governance
- Tournament

Who am I?

MSc in Accounting and Finance, The University of Melbourne, Australia (2017-2019)

- H1, Dean's Honour List

BSc in Accounting, Xiamen University, China (2013-2017)

Who are you?

Your background?

Your major?

Your expectations for this course?

Learning outcomes:

- Deepen knowledge of financial and non-financial reporting standards
- Understand the importance of integrated reporting to management and investors;
- Understand the interconnections between the financial and non-financial drivers of performance and the impact of ESG factors
- Learn the principles for responsible investing (PRIs)
- Discuss some literature references on reporting and sustainability.

Program:

1. Financial reporting framework
2. Main international financial reporting standards
3. Financial analysis and interpretation
4. Non-financial reporting: adapting to new demands and challenges
 1. ESG reporting
 2. Frameworks and standards
 3. Materiality and stakeholder engagement
 4. Principles for Responsible Investment Decisions
5. Integrated reporting systems and metrics
 1. Sustainable Balanced Scorecard
 2. Financial and non-financial KPI

Evaluation:

Regular Season:

Final grade includes:

- Individual written test with a minimum grade of 8 points (60%);
- Group work on Sustainability Reporting (40%).

Objective of this class:

1. Financial reporting
2. Value reporting and Investor relations dashboards
3. Main international financial reporting standards-IFRS
4. Conceptual Framework for Financial Reporting

Reading:

Main reading:

Rankin, M., Ferlauto, K., McGowan, S., & Stanton, P., 2022. *Contemporary Issues in Accounting*. 3rd ed. Australia: Cengage. ISBN 978-0-730-39782-3.

- Chapter 3 and 11

Supplementary reading:

International Financial Reporting Standards (IFRS), 2018. *Conceptual Framework for Financial Reporting*. London: IFRS Foundation.

What Is Financial Reporting?

- Formal records that provide in-depth insights into financial information.
- Financial results of an organization that are released to stakeholders and the public.
- Key function of the controller, who may be assisted by the investor relations officer if an organization is publicly held.



Why Is Financial Reporting Important?

- 1st - It is legally required for tax purposes.
- 2nd - Give investors, creditors and other businesses an idea of the financial integrity and creditworthiness of your company.
- 3rd - Provides a comprehensive snapshot for stakeholders to make better informed business decisions (internal and external).
- 4th - Serve as the 'bedrock' for other reports that CAN and SHOULD be used to make decisions.



Enron's collapse

About Enron:

<https://www.youtube.com/watch?v=SMT5v5zT5KQ>

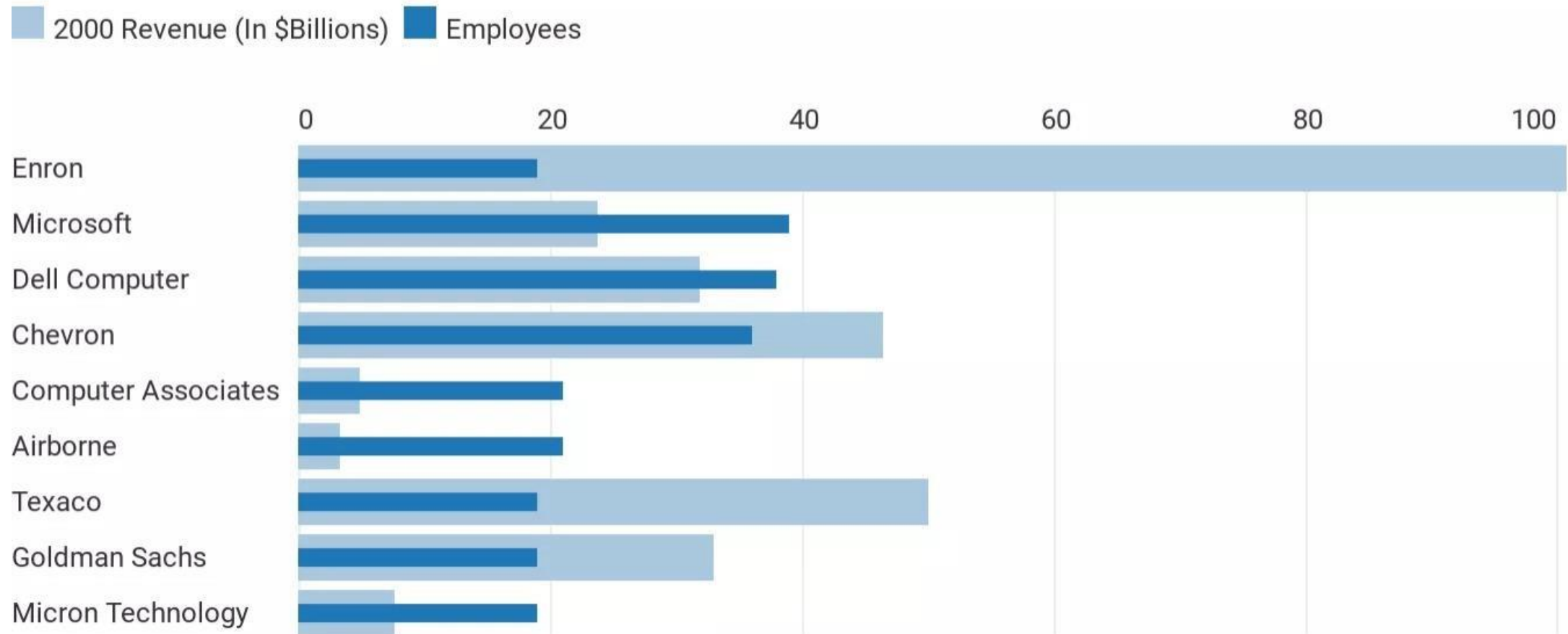
<https://youtu.be/CH0p2ST8H5E>

About other accounting scandals:

<https://corporatefinanceinstitute.com/resources/knowledge/other/top-accounting-scandals/>

Enron's financial reporting

Too good to be true?



Enron's collapse

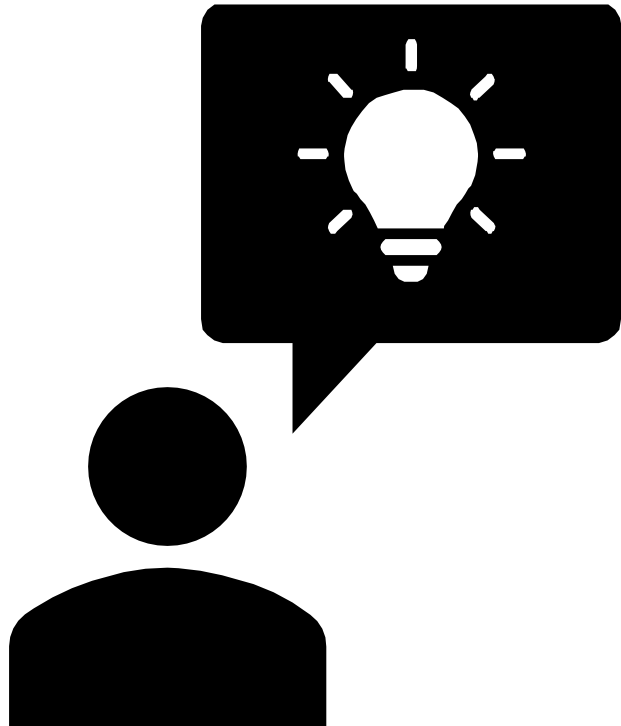
Enron Share Price, Jan 2000-Dec 2002



The Benefits of Financial Reporting

- **Raise and manage funds** (more accurately)
- **Improved debt management** (gauge liquidity)
- **Trend identification** (tackle potential weaknesses)
- **Real-time tracking** (avoiding any potential roadblocks)
- **Liabilities** (test for credit capacity)
- **Progress and compliance** (improve efficiency and compliance)
- **Improved internal vision** (reflect upon strategy)
- **Communication** (sharing critical financial information throughout your organization)

4 Use-Cases For Financial Reporting



1. Is purchasing this stock a good idea?

- If you're considering investing in as an individual or on behalf of your current organization, financial reporting analysis can give you some data that will help you make your decision.
- This is also one way you can gain insight into whether a company is potentially under- or overpriced in the stock market.

4 Use-Cases For Financial Reporting

2. Are we profitable? Will we be in the future?

- This is crucial information.

3. How much cash 'runway' do we currently possess?

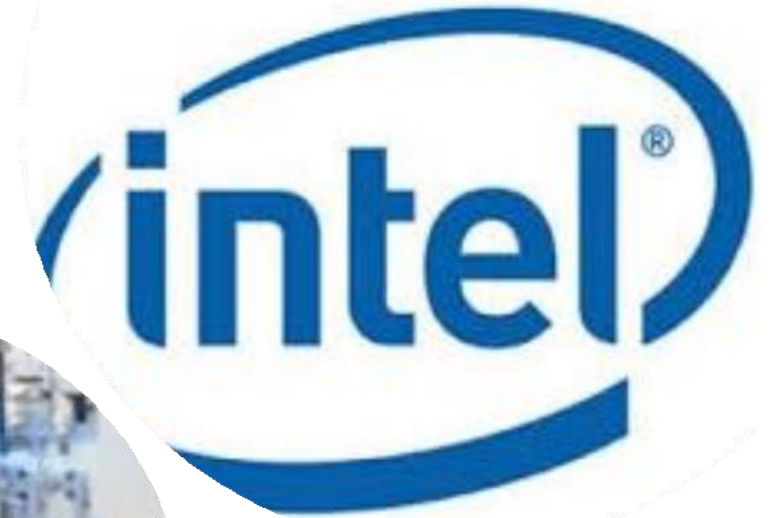
- Cash is oxygen to a business
- Some companies, [like Apple](#), like to sit on colossal amounts of cash.



4 Use-Cases For Financial Reporting

4. Do we have the capital to invest in new lines of business?

- Other companies prefer to invest their money, sometimes in a long-term basis. For instance, Intel upgrade their factories and equipment on a regular basis.



Group discussion: Is It Always Good to Have Transparent Disclosure?

Healy, P. M., & Palepu, K. G. (2001). Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical disclosure literature. *Journal of accounting and economics*, 31(1-3), 405-440.

Value reporting

Public revelations call up the fears of accountability and competitive exposure.

But in today's marketplace:

- ✓ Greater transparency and better disclosure are keys to shareholder value.
- ✓ A company is more apt to be successful in achieving its goals if the goals are made public.
- ✓ It's important to avoid pitfalls like missing relevant market information and the non-financial measures that drive value.

Today, financial reporting represents a shrinking percentage of the information that the market considers important.

“In a perfect world, investors, board members, and executives would have full confidence in companies’ financial statements... Unfortunately, that’s not what happens in the real world, for several reasons.”

Sherman and Young (2016). Where Financial Reporting Still Falls Short, Harvard Business Review.

Without broader value drivers, we are stuck with the "Earnings Game." This is a game played in the press and by the sell-side analysts, whose main focus is on a company's short-term performance and its reported earnings

Tom Chambers is president of Senior Partner Services and a former partner at PriceWaterhouseCoopers, where he was a member of a global task force on value reporting.

Value reporting

Firms need to supplement historic financial information with more information about value-building activities and non-financial performance measures with predictive value.



Value-Reporting model is about broadening corporate reporting to have companies identify and meet analysts' and investors' needs for relevant information about value drivers, intangible assets and estimated future cash flows.



Whereas it's easier to report earnings-per-share, it's more difficult to crisply and objectively report value drivers like customer satisfaction, brand recognition and market share (with high predictive value).

Value reporting

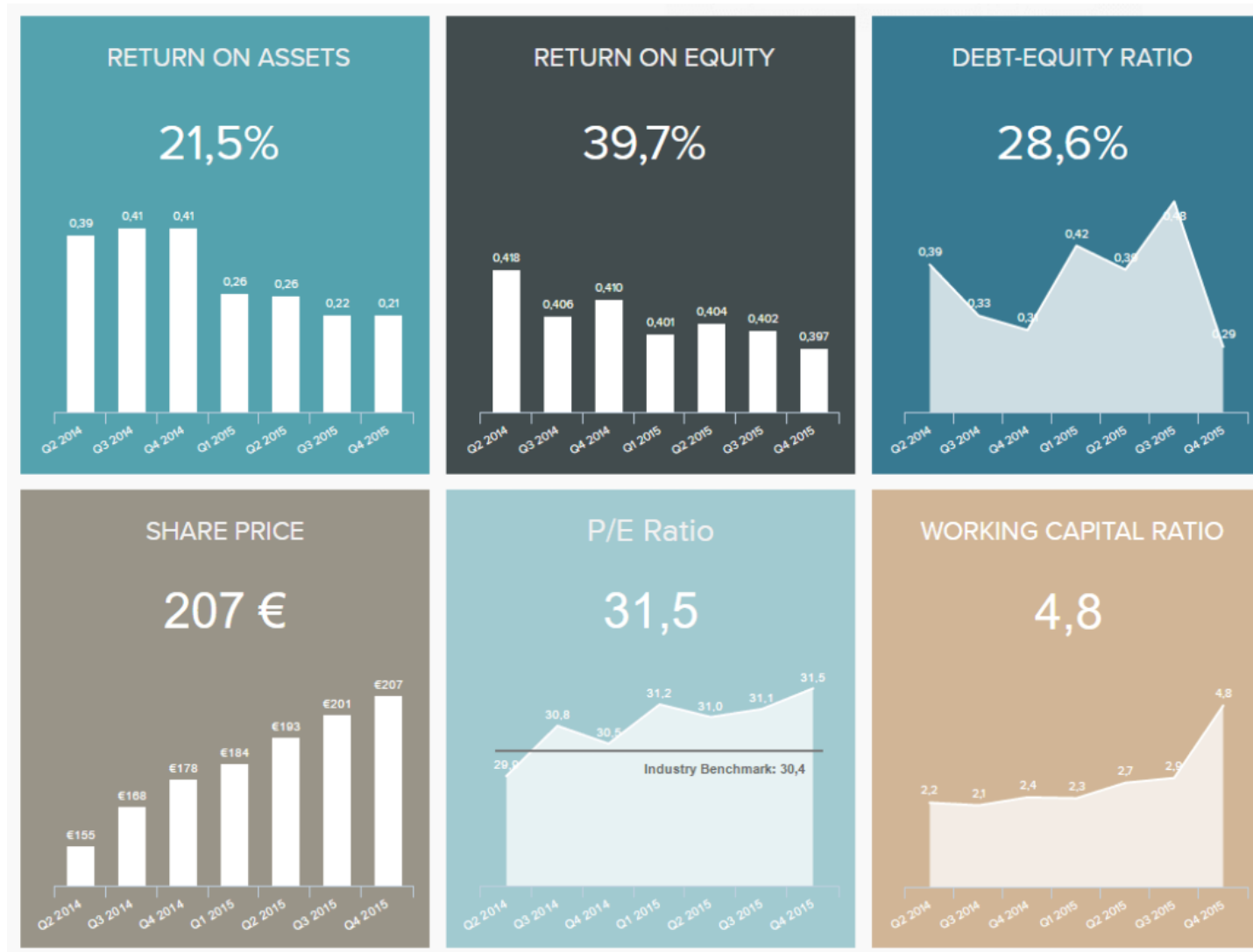
Each industry has different business drivers that help drive value creation.

For example, in the high-tech industry what are the top ten list of relevant value drivers?

- financial measures: earnings, cash flow and gross margins.
- nonfinancial measures: strategic direction, quality/experience of the management team and speed to market.
- macro measures: competitive landscape, market size, market growth and market share



Investor relations dashboards



Revenue and customer overview

Revenue Actual vs Target

€ 675.706

Actual
Revenue

€ 580.460

Target
Revenue



116%

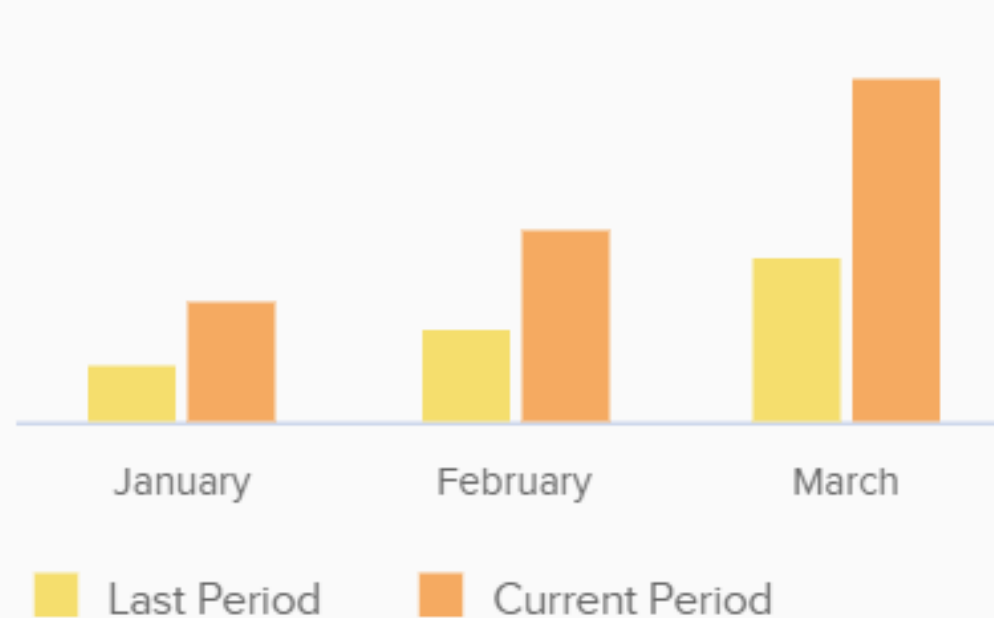
Target
Achievement

Revenue compared to previous Year

€400k

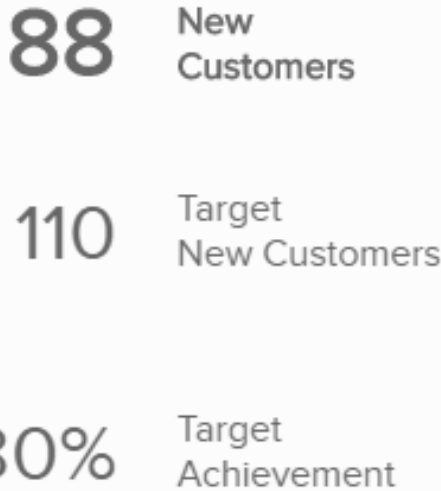
€200k

€0k

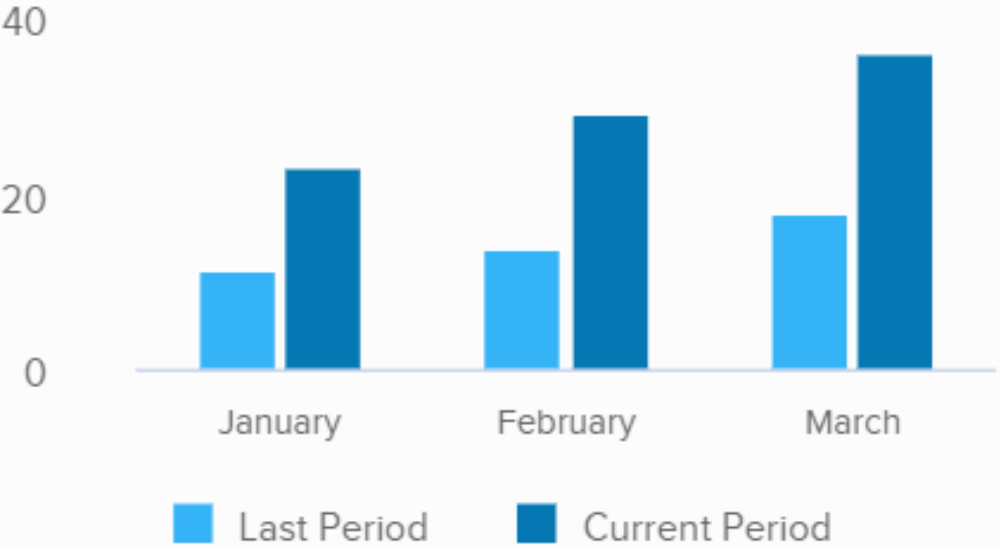


Revenue and customer overview

of New Customers Actual vs Target



of New Customers compared to previous Year



Revenue and customer overview

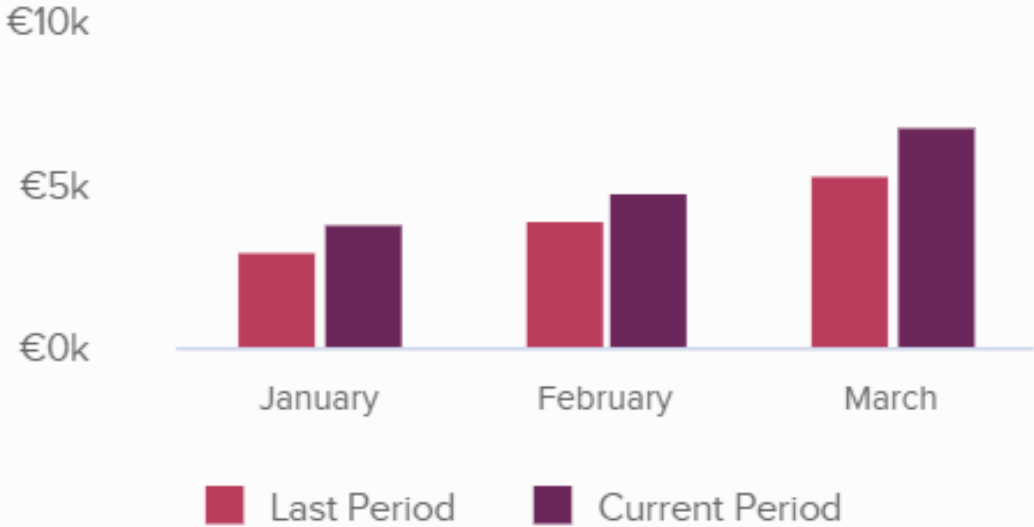
Avg. Revenue per Customer Actual vs Target

€ 5.150 Actual Revenue

€ 5.006 Target Revenue

✓ 116% Target Achievement

Avg. Revenue per Customer compared to previous Year





GROSS PROFIT MARGIN



OPEX RATIO



OPERATING PROFIT MARGIN



NET PROFIT MARGIN

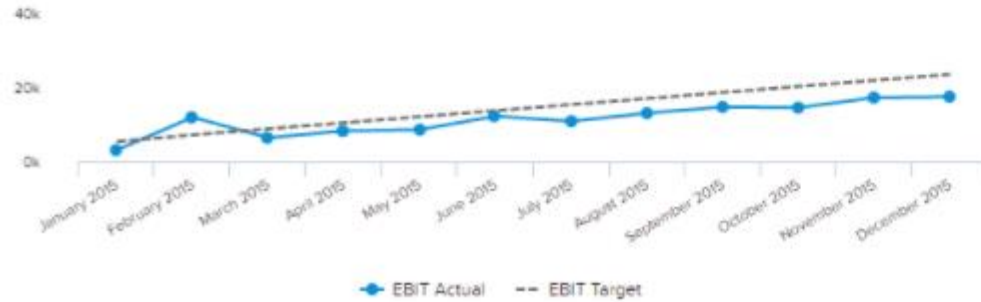
OPEX

Month-to-Month | YTD



Earning before Interest and Taxes

Month-to-Month | YTD



INCOME STATEMENT

Revenue	567.304	\$
COGS	119.129	\$
GROSS PROFIT	448.170	\$
OPEX	326.519	\$
Sales	193.760	\$
Marketing	66.382	\$
General & Admin	66.358	\$
Other Income	1.448	\$
Other Expenses	6.823	\$
OPERATING PROFIT (EBIT)	116.257	\$
Interest and Tax	25.015	\$
NET PROFIT	91.264	\$

FINANCIAL PERFORMANCE DASHBOARD

RETURN ON ASSETS



WORKING CAPITAL RATIO



RETURN ON EQUITY



DEBT-EQUITY RATIO

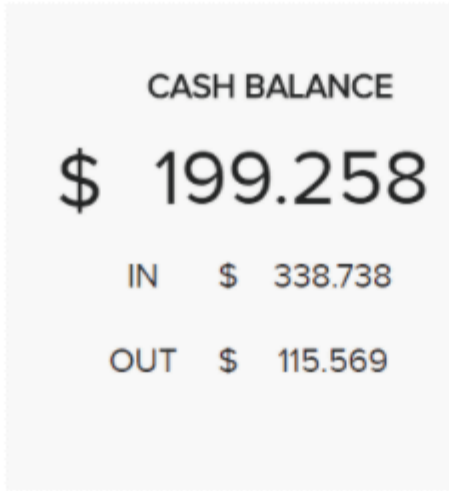
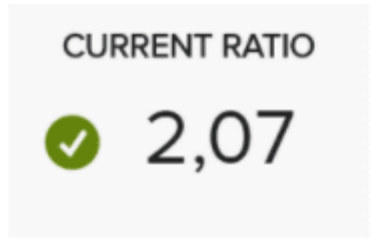
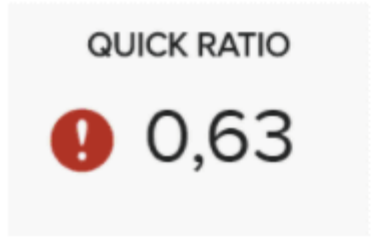


BALANCE SHEET

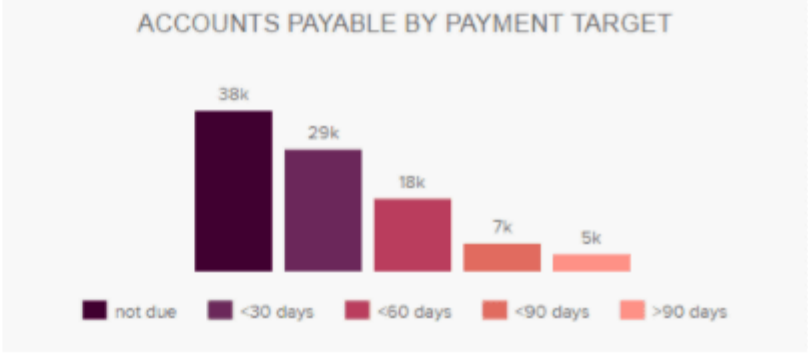
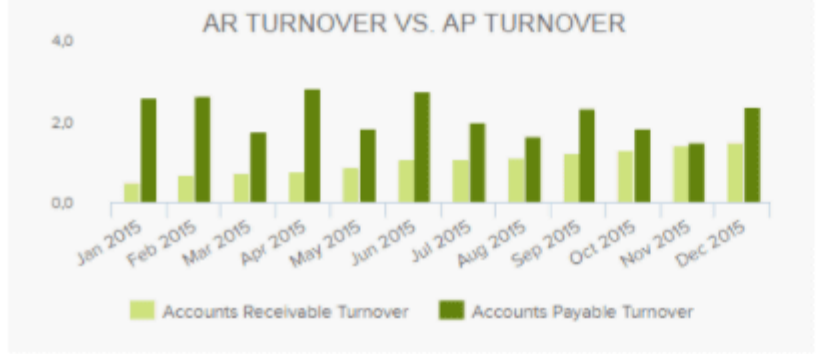
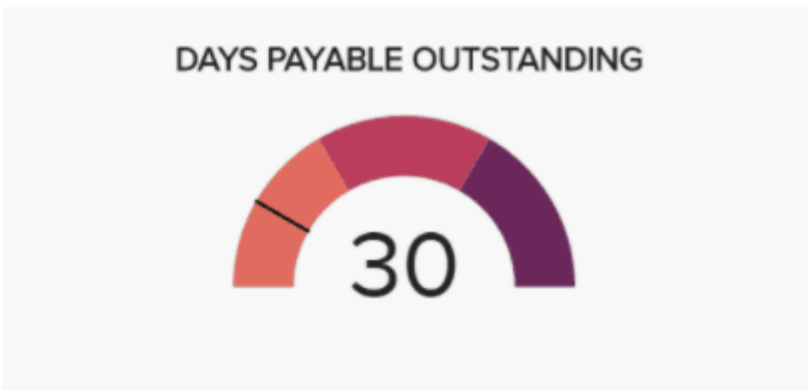
TOTAL ASSETS	€ 2.825.371	
Current Assets	€ 1.945.371	
Cash	€ 497.683	
Accounts Receivable	€ 915.422	
Inventory	€ 532.263	
Long-Term Assets	€ 880.000	
TOTAL LIABILITIES	€ 2.825.371	
Current Liabilities	€ 610.106	
Accounts Payable	€ 418.166	
Other Liabilities	€ 191.941	
Shareholder Equity	€ 1.446.620	
Common Stock	€ 998.750	
Current Earnings	€ 447.870	

CASH DASHBOARD | last year

WORKING CAPITAL



CASH CONVERSION



Let's get into groups!!

Organize in 8 groups
5-6 students per group

Fill in the group form:

- Group number
- Student name
- Student ID
- Student email address



A single set of high quality, global accounting standards

“

The World Bank has been a long-term supporter of work to develop a single set of high-quality global accounting standards.

World Bank, 2017

“

[The FSB] reiterated its support for...a single set of high quality global accounting standards.


FSB declaration, 2015

“

We support continuing work to achieve convergence to a single set of high quality accounting standards.

G20 leaders' declaration, 2012


WHY?



A single set of
high quality,
global accounting
standards – why?


- Modern economies rely on cross-border transactions.
- More than a third of all financial transactions occur across borders.
- Investors seek investment opportunities across the world
- Companies raise capital, undertake transactions or have international operations in multiple countries.

<https://www.youtube.com/watch?v=gcqMq0BEDW0>



A single set of
high quality,
global accounting
standards – why?

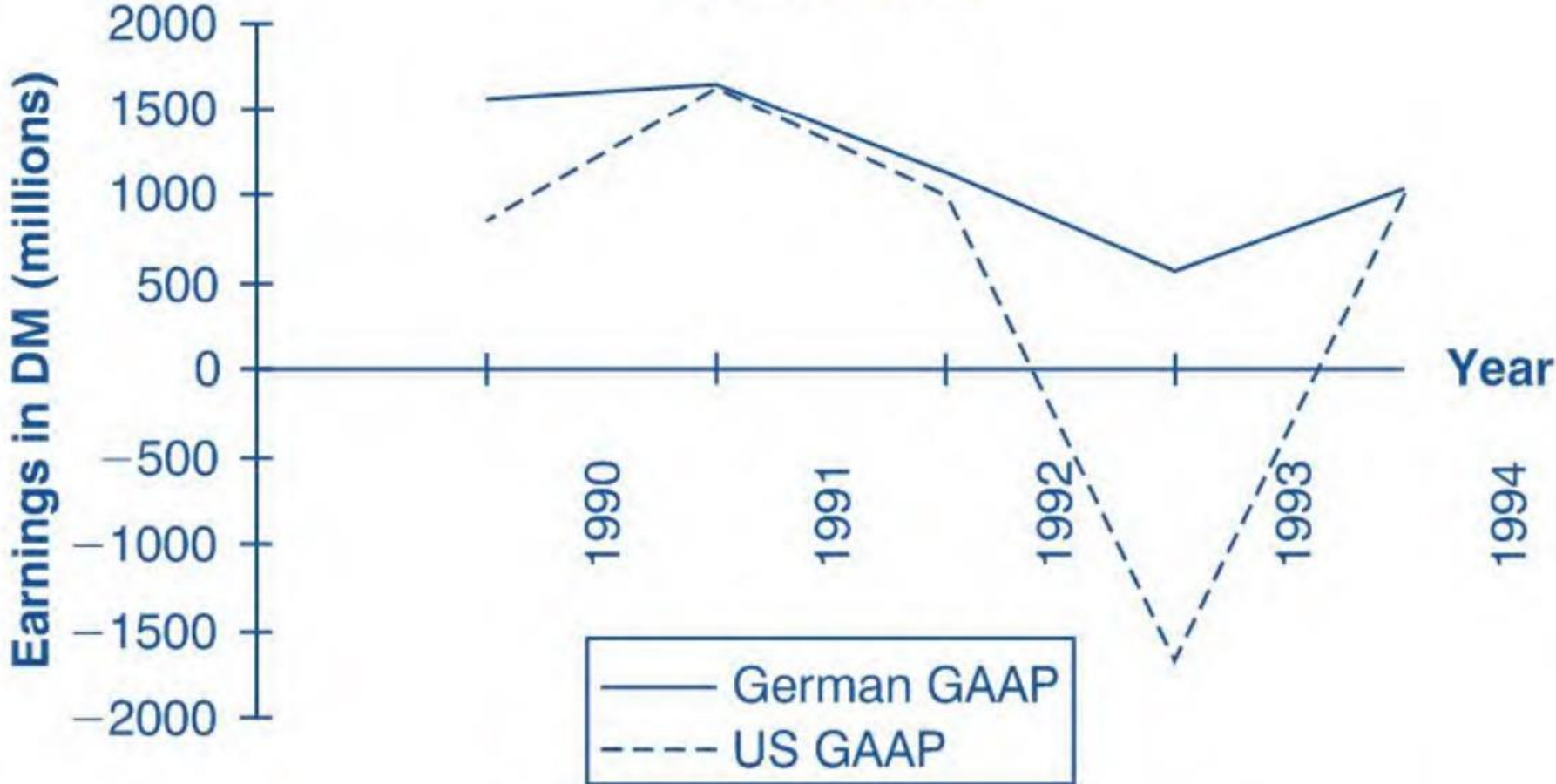
- Different countries will have different:
 - Political philosophies and objectives.
 - Levels of economic growth and development.
 - Economic systems.
 - Legal systems.
 - Codified or civil law.
 - Common law.
 - Culture
- All of which will influence accounting practice.



A single set of
high quality,
global accounting
standards – why?

- Worldwide accounting diversity creates challenges for international business operations and investment.
- It is costly for multinational enterprises to restate their accounts to meet the requirements of every jurisdiction in which they report.
- Investors also incur costs in comparing results of companies when their financial reports are prepared using different rules.

Daimler-Benz



Frameworks for financial reporting

Two main ways that financial reports are standardized:

- 1)** The **GAAP** (Generally Accepted Accounting Principles). This is the system used by the United States, and almost no one else (just like the Imperial measurement system!).
- 2)** The **IFRS** (International Financial Reporting Standards). This system is utilized by several countries around the world, including Canada, Australia, India, and China.

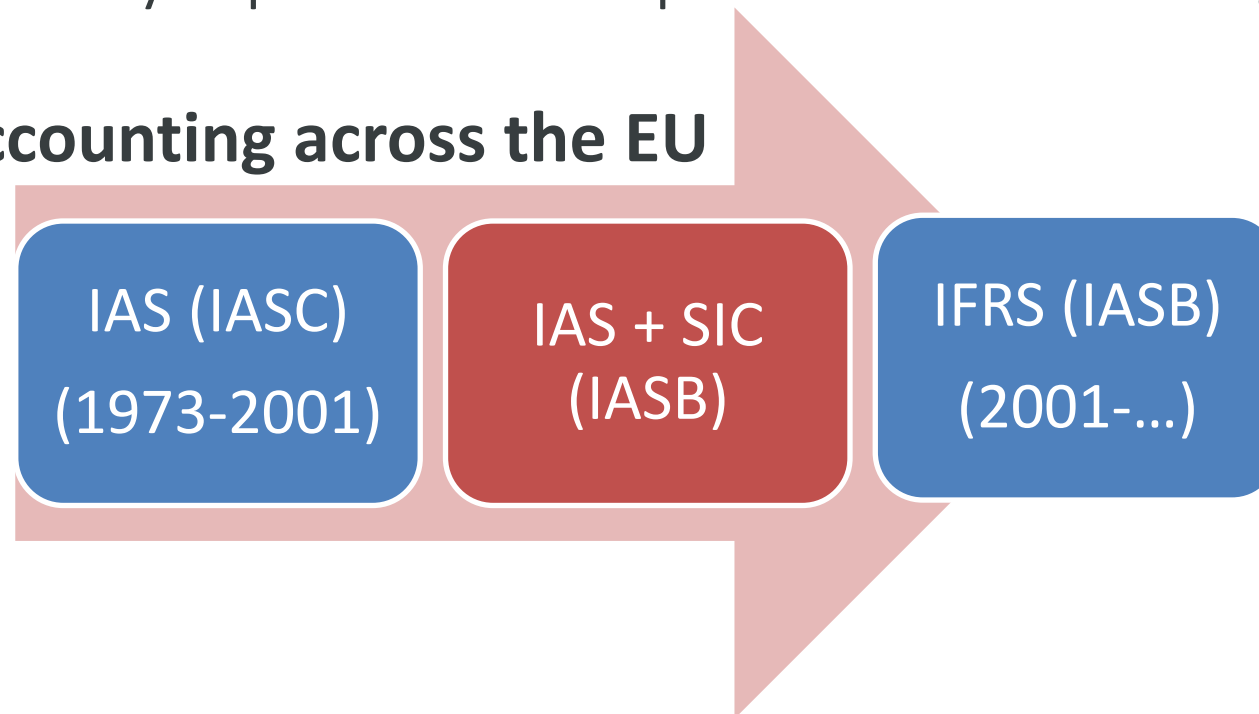
... And one critical element to consider when working with EU-based data of any kind:

-The GDPR: (The General Data Protection Regulation): Came into effect on 25th May, 2018, designed to modernize the laws that protect the personal information of individuals

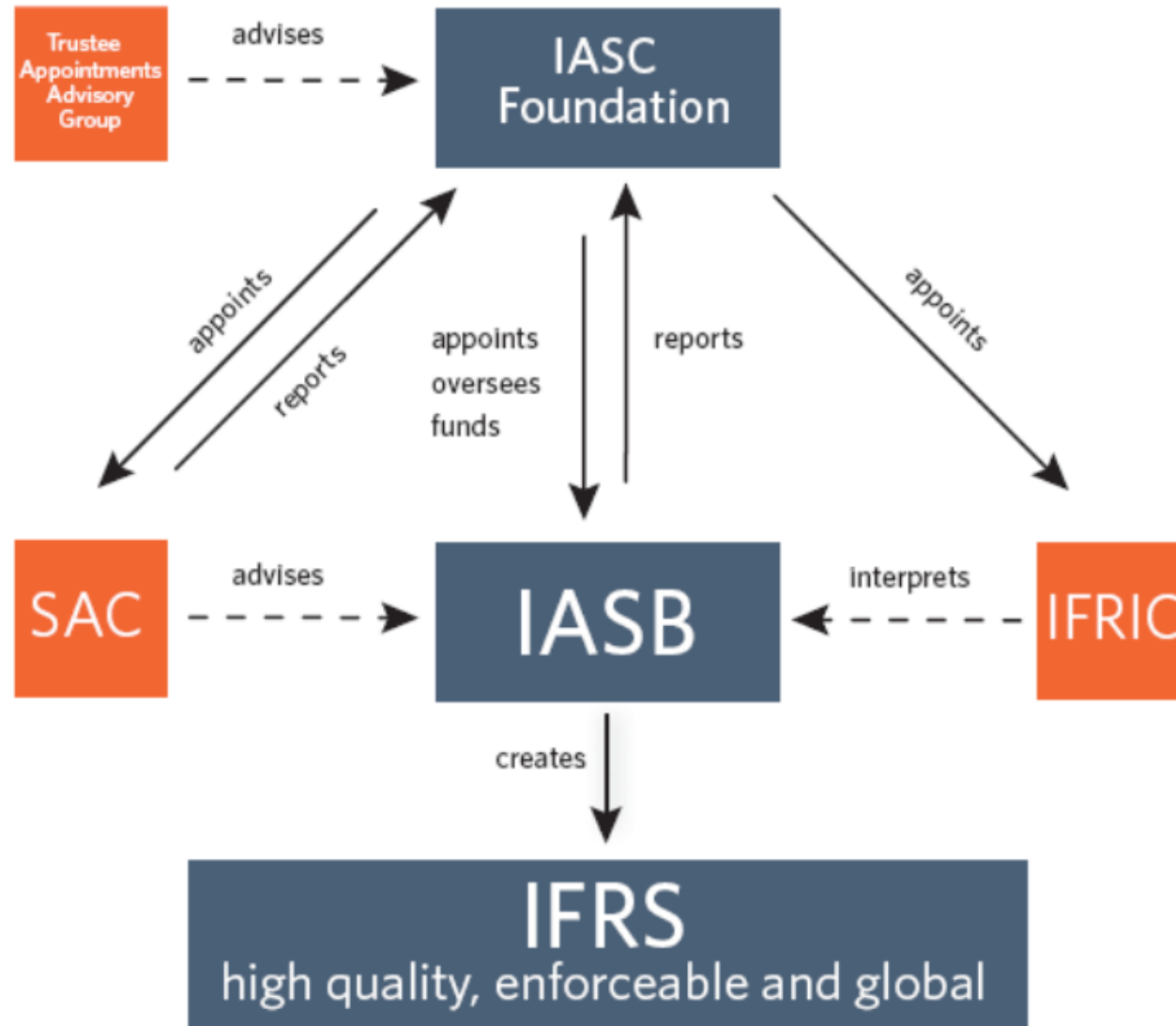
The framework for financial reporting: IFRS

- The IFRS began as an attempt to harmonize accounting across the European Union, but the value of harmonization quickly made the concept attractive around the world.
- They are progressively replacing the many different national accounting standards - it's the most common global set of standards.
- The IFRS is particularly important for companies that have dealings in several countries.

Harmonize accounting across the EU

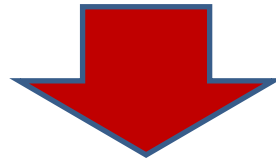


...
**Synchronizing
accounting standards
across the globe is an
ongoing process**





Set of guidelines to determine how transactions and other accounting events are required to be reported in financial statements. IFRS are used in at least 120 countries, as of 2020, including those in the EU and many in Asia and South America.



Navigator: <https://www.ifrs.org/issued-standards/list-of-standards>

IFRS Standards around the world: where are they required for domestic companies?



Explore it!!

Whether companies in your country adopt IFRS?

Filter

All

Filter



<https://www.ifrs.org/use-around-the-world/use-of-ifrs-standards-by-jurisdiction/>

Who must adopt IFRS?

Regulation (EC) No 1606/2002 requires **all listed companies to prepare their consolidated financial statements in accordance with IFRS** (international financial reporting standards), previously known as IAS (international accounting standards).

What is included?

For publicly held corporations, financial reporting can be very detailed and complex. It typically encompasses:

- financial statements;
- extensive footnotes disclosures (according to framework);
- management assessments or reports;
- management discussion and analysis (MD&A);
- notes providing details about each item on the balance sheet, income statement, and cash flow statement, including insights into the accounting method used;
- assurance opinions.

A single set of high quality, global accounting standards

Benefits of IFRS Standards:

- Financial statements are consistent, reliable, transparent and comparable across all companies, market sectors and countries;
- Trust and confidence for investors;
- Common accounting language;
- Accuracy, consistency, and comparability in financial results.

A single set of high quality, global accounting standards

Benefits of IFRS Standards:

- bring **transparency** by enhancing the international comparability and quality of financial information;
- strengthen **accountability** by reducing the information gap;
- contribute to economic **efficiency** by helping investors to identify opportunities and risks across the world, thus improving capital allocation.

Any downside of IFRS adoption?

Conceptual Framework for Financial Reporting

What is it?

- A **conceptual framework** is a group of ideas or principles used to plan or decide something.
 - Not only found in accounting, used in many areas to establish guidelines, make decisions or solve problems
 - Often include broad principles, which can apply across a wide range of situations or circumstances

Conceptual Framework for Financial Reporting

What is it?

- **Accounting conceptual framework:**
 - A normative theory (states what should happen).
 - It prescribes the basic principles that are to be followed in preparing financial statements.
 - It is a coherent system of concepts, which are guidelines to the accounting standards used for financial reporting.
 - guidelines to the accounting standards used for financial reporting.

Conceptual Framework for Financial Reporting

What is it?

Chapter 1	The objective of financial reporting
Chapter 2	Qualitative characteristics
Chapter 3	Financial statements and the reporting entity
Chapter 4	Elements (including asset, liability, equity, income and expenses)
Chapter 5	Recognition and derecognition
Chapter 6	Measurement
Chapter 7	Presentation and disclosure
Chapter 8	Concepts of capital and capital maintenance

Conceptual Framework for Financial Reporting

#1 – The objective of general purpose financial reporting

The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity. Those decisions involve decisions about:

(a) buying, selling or holding equity and debt instruments;

(b) providing or settling loans and other forms of credit;

Or (c) exercising rights to vote on, or otherwise influence, management's actions that affect the use of the entity's economic resources.

Conceptual Framework for Financial Reporting

#2 - Qualitative characteristics:

Fundamental characteristics

- Relevance / Materiality
- Faithful representation

Enhancing characteristics

- Comparability
- Verifiability
- Timeliness
- Understandability

Conceptual Framework for Financial Reporting

Faithful representation

- Complete
- Neutral
- Free from error

Conceptual Framework for Financial Reporting

#3 - Financial statements: objectives and scope

A complete set of financial statements includes:

- reports on a company's assets, liabilities and owners' equity at a given point in time.

Statement of
financial
position



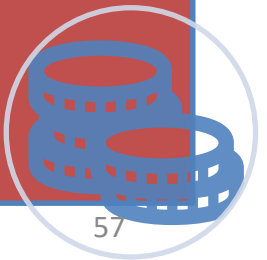
- reports on a company's income, expenses, and profits/losses over a period of time.

Statement of
profit or loss



- reports on a company's cash flow activities, including its operating, investing and financing activities.

Statement of
cash flows



To understand
the financial
statements,
also look at IAS 1

Presentation of Financial Statements

Purpose?

“...provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Financial statements also show the results of the management’s stewardship of the resources entrusted to it.”

#4 - Elements of financial statements

Item discussed in Chapter 1	Element	Definition or description
Economic resource	Asset	A present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits.
Claim	Liability	A present obligation of the entity to transfer an economic resource as a result of past events.
	Equity	The residual interest in the assets of the entity after deducting all its liabilities.
Changes in economic resources and claims, reflecting financial performance	Income	Increases in assets, or decreases in liabilities, that result in increases in equity, other than those relating to contributions from holders of equity claims.
	Expenses	Decreases in assets, or increases in liabilities, that result in decreases in equity, other than those relating to distributions to holders of equity claims.
Other changes in economic resources and claims	—	Contributions from holders of equity claims, and distributions to them.
	—	Exchanges of assets or liabilities that do not result in increases or decreases in equity.

Financial position

Financial performance

Source: Conceptual Framework

Conceptual Framework for Financial Reporting

#4 - Elements of financial statements (revised in 2018)

Assets

Previous definition	New definition
A resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity	A present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits

Conceptual Framework for Financial Reporting

#4 - Elements of financial statements (revised in 2018)

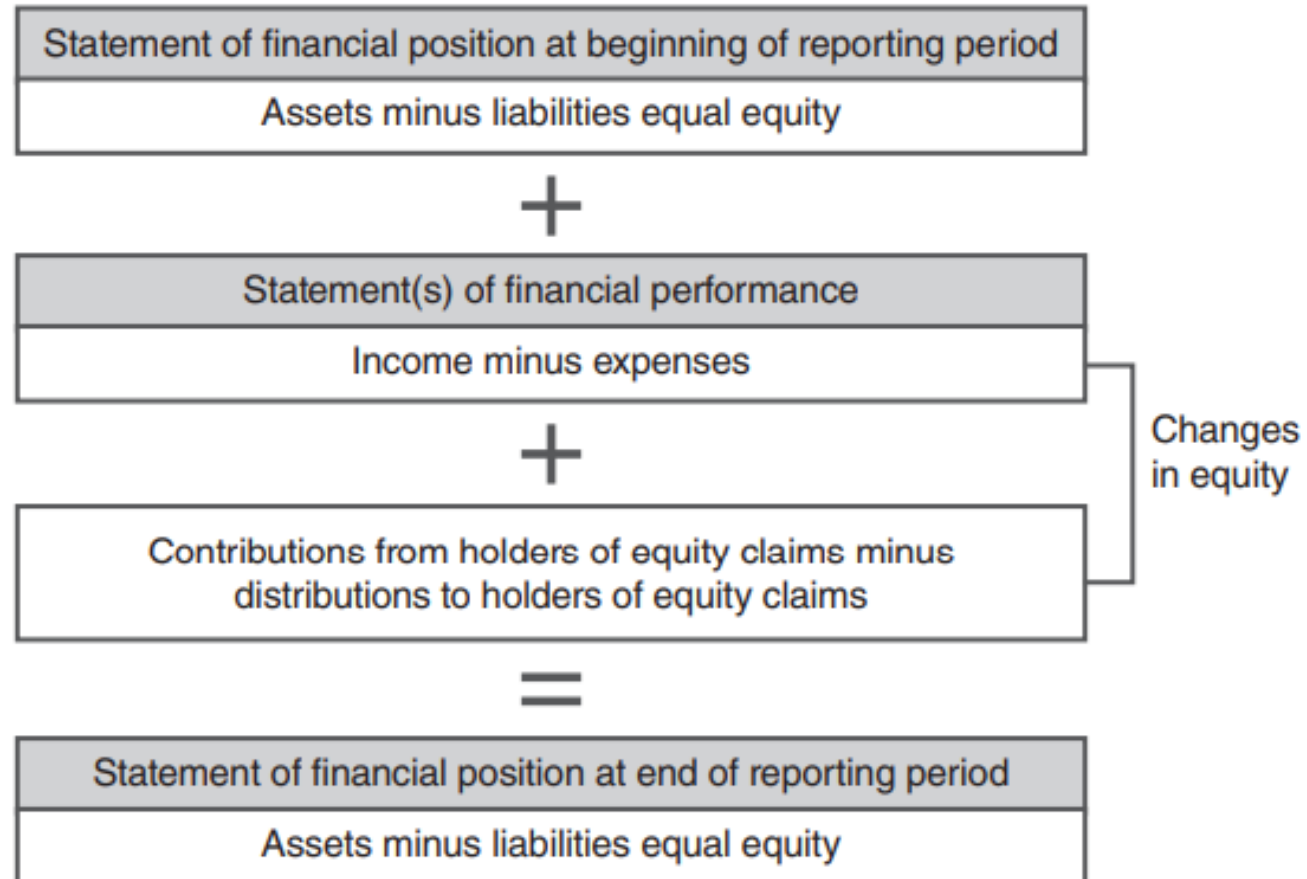
Liabilities

Previous definition	New definition
A present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits	A present obligation of the entity to transfer an economic resource as a result of past events. An obligation is a duty of responsibility that the entity has no practical ability to avoid

Equity is still defined as the residual interest in the assets of an entity after deducting all the liabilities.

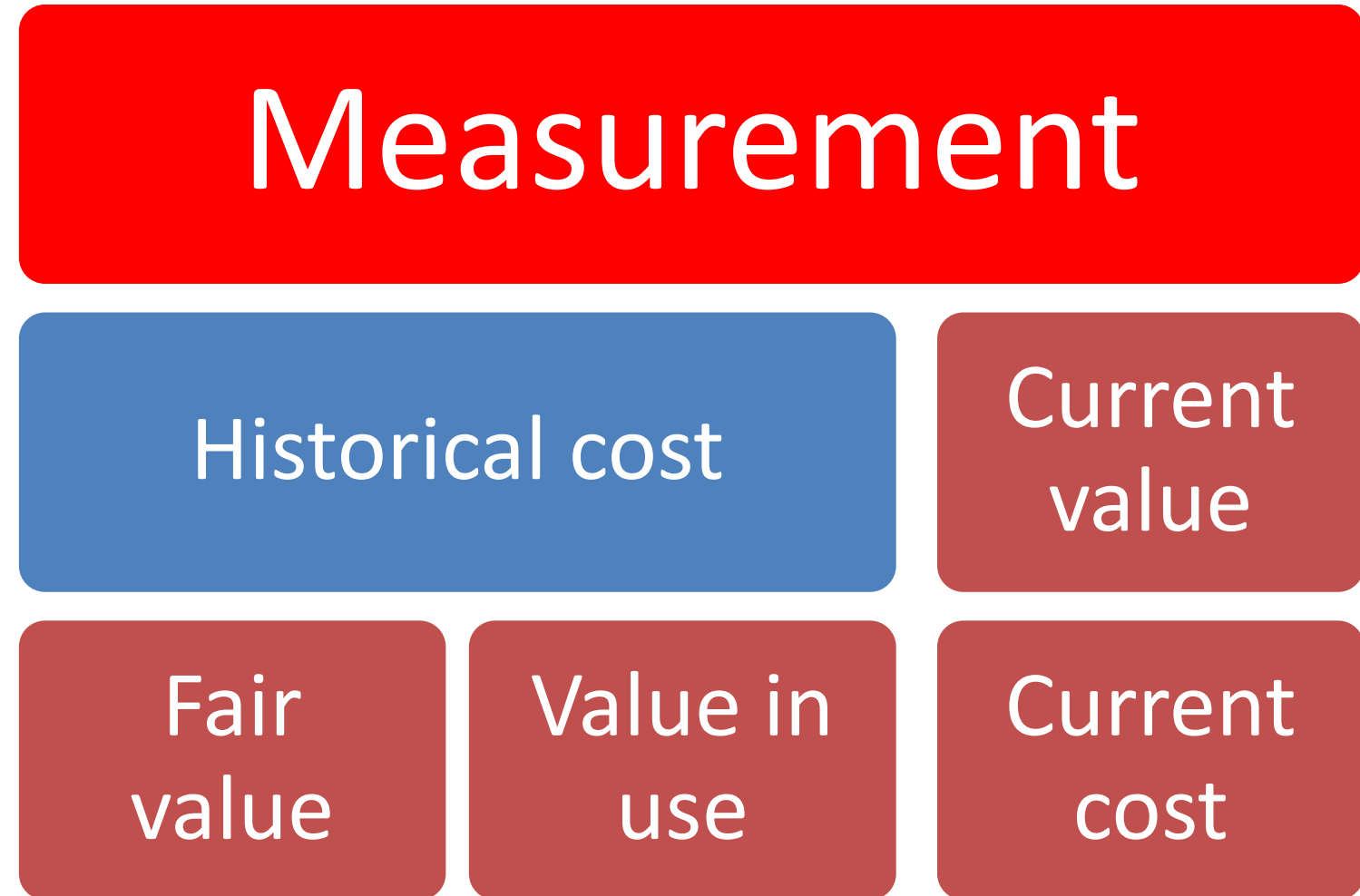
Conceptual Framework for Financial Reporting

#5 – Recognition



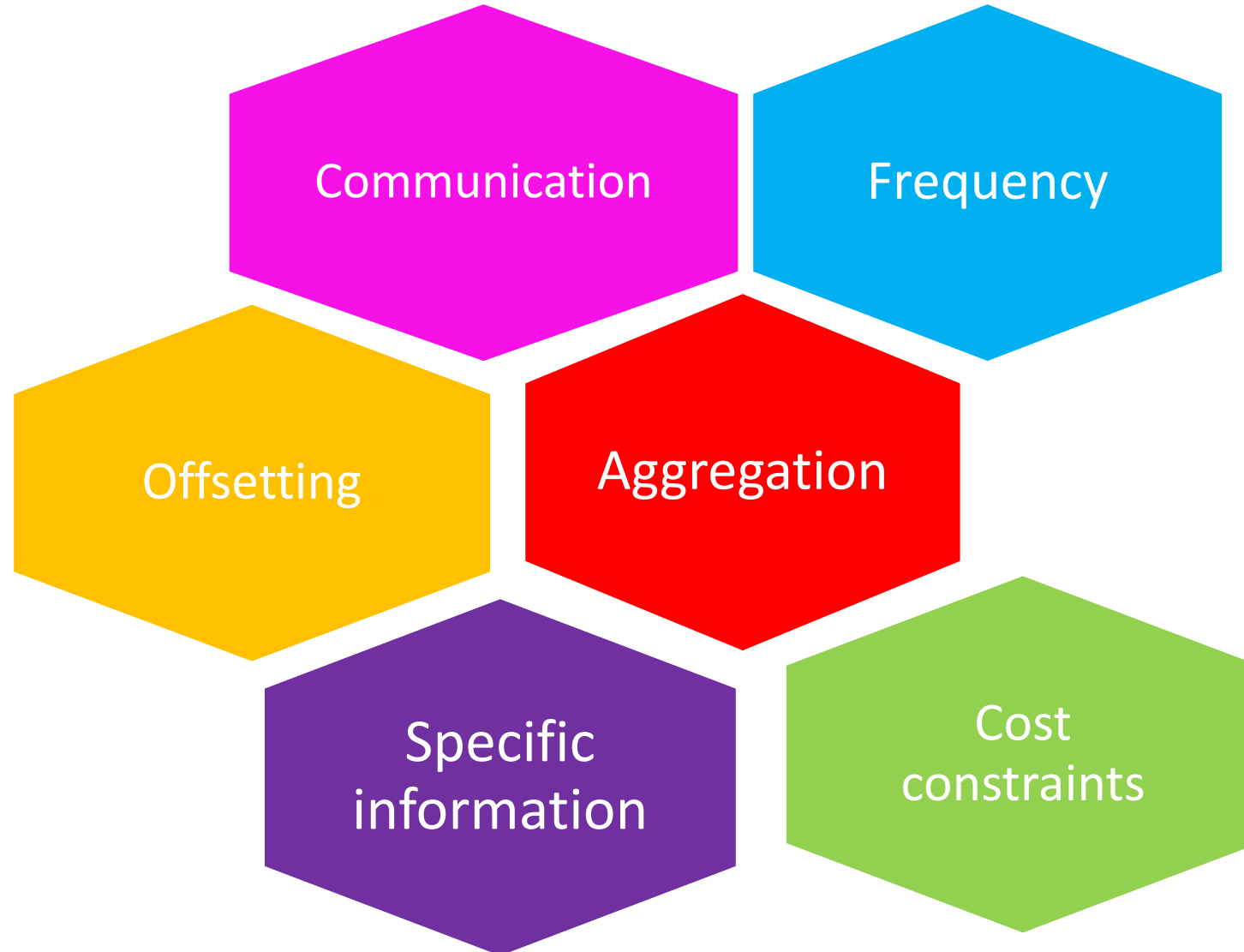
Conceptual Framework for Financial Reporting

#6 – Measurement



Conceptual Framework for Financial Reporting

#7 – Disclosure



Problems with and criticisms of the Conceptual Framework?

Summary:

1. Financial reporting
2. Value reporting and Investor relations dashboards
3. Main international financial reporting standards-IFRS
4. Conceptual Framework for Financial Reporting

Questions?