# Sense-Making and Sense-Giving: Reaching Through the Smokescreen of Sustainability Disclosure in the Stock Market

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## Financial Analysts Face a Smokescreen of Sustainability Information

Despite the increased focus on sustainability information in the information flow surrounding the valuation of companies, our knowledge is rather limited regarding how the financial analysts' sense-making and sense-giving of such information affect their work of interpreting, assessing and communicating value-added information to investors. This chapter sets out to enhance our knowledge in this vital area by exploring analysts' cognitive frames. We argue that the complex and

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ambiguous nature of sustainability information implies that the analysts are faced with a smokescreen challenging their sense-making and sense-giving processes (Weick 1995; Weick et al. 2005) of their important task to produce relevant and credible investment advices to their clients, i.e. the investors. In order to make informed investment decisions, investors need to be able to make appropriate valuations of companies and also understand their underlying value-creating mechanisms. Nevertheless, investors may not have time or competences to search for, evaluate and draw conclusions on potential investment opportunities. This is where professional financial analysts and management teams enter into the sophisticated exchange of corporate information. To enable efficient investment decisions and assessment of company potential, there is a need for relevant and credible information such as information on the company's operations, future strategies, risks, competitors, skills and patents. In this sophisticated exchange of corporate information, the management team is the core information provider or supplier of information to analysts (information intermediaries) and to investors (information demanders) (Arvidsson 2003; Johansson 1998, 2004). To understand the prerequisites for an efficient allocation of resources in the stock market, it is not only vital to acknowledge the roles of these key actors (management teams, financial analysts and investors). It is also important to identify different types of corporate information (financial information and non-financial information including sustainability information) and acknowledge the challenges that corporate information in general and sustainability information in specific mean in a transparency and information asymmetry perspective. Before we dig deeper into the analysts' sense-making and sense-giving processes and how they are affected by the increased focus on sustainability in corporate reports (sects. "The Cognitive Foundations: An Introduction to the Concepts", "Analysts' Cognitive Frames in the Early 2000s" and "A Shift Towards Enhances Cognitive Legitimacy in Sense-Making and Sense-Giving"), we will in the sections below, outline corporate information and corporate disclosure from a transparency and information asymmetry perspective.

## Corporate Financial Information and Non-financial Information: The Birth of Sustainability Information

In all countries, there are laws and regulations requiring companies to disclose certain corporate to stakeholders such as investors and analysts. Corporate information is provided in corporate reports, i.e. the annual or integrated reports. We usually refer to this information as corporate *financial* information. It has a long tradition. The double-bookkeeping has roots in the thirteenth century when the monk Luca Pacioli invented this intriguing system for companies to keep track of their financial situation with help of the double-entry bookkeeping system.[1] Corporate financial information is a language of business; items and structure of the balance sheet, income- and cash-flow statements are familiar and understood both by management and by analysts. Also, the key performance indicators (KPIs) or financial measures like solvency, profitability and turnover are well-known and provide relevant information for assessing the performance of a company.

In 1987, the Brundtland Report entitled "Our common future" (UNWCED 1987) was published with the objective of drawing attention to the global need for sustainable development. The idea was to trigger companies to speed up their transformation of becoming more sustainable organizations. Consequently, companies started, however, quite slowly to disclose more information on how they performed on the sustainability arenas. This became a new type of non-financial information. A well-established definition of sustainability is that it includes information on social, environmental and economic aspects (UN 2018). Today, the integration of such sustainability information into corporate communication domain has become vital and is a topic high up on the agendas in politics, business society and the academia (Dameri and Ricciardi 2015, p. 861; Malmström et al. 2017). The environmental and social scandals taking place have served as triggers in establishing laws and regulations forcing companies to no longer merely consider economic aspects into measurement of performance (Massaro et al. 2018).

As discussed in chapter "An Exposé of the Challenging Practice Development of Sustainability Reporting: From the First Wave to the EU Directive (2014/95/EU)" in this book, there is an increasing corporate trend to engage in sustainability reporting, i.e. disclosure of sustainability information to external stakeholders. The soft information on social and environmental concerns has become more and more central, and specifically the integration of these aspects into business models and value chains (Foote et al. 2010; Wasiluk 2013). Studies show that companies integrating sustainability actions into the business model increase their reputation (Dutot et al. 2016), improve their image (Pedrini 2007) and enhance innovation capabilities (Chang and Chen 2012).

Sustainability reporting has also attracted interest from research society (see Cho et al. 2015; Dienes et al. 2016; Hahn and Kühnen 2013; Parker 2005; Patten 2013), for instance focusing on the value relevance of sustainability information (see Cahan et al. 2016; Dhaliwal et al. 2012).

## Corporate Disclosure: A Remedy for Decreasing Information Asymmetry in the Information Flow

In the quest of decreasing information asymmetry (Akerlof 1970) and contributing to a fair valuation of the company, the management team provide corporate information to external stakeholders. Corporate information is primarily provided *indirectly* via, e.g. corporate reports, website, marketing materials, brochures and interviews. To a more limited extent, corporate information is disclosed *directly* to certain stakeholders (primarily analysts and investors) via private meetings, conferences and general annual meetings (Johansson 2004).

The management team is faced with a trade-off situation between disclosing and withholding information. Disclosing too much information might be unwise due for proprietary reasons and diminishing returns (Hallvarsson 2009; Johansson and Malmström 2013). However, the information flow between the insiders of a company and the outsiders, i.e. external stakeholders (including financial analysts), is characterized by asymmetric information (Akerlof 1970). This means that those outside the company, e.g. analysts and investors, are faced with a smokescreen

regarding what is really going on inside the company. Thus, the presence of asymmetric information impairs the analysts' valuation process. The literature is full of examples of why a management team should try to decrease the level of asymmetric information in the information flow by disclosing information. According to empirical studies, the advantages with decreased information asymmetry are lower cost of equity (Dhaliwal et al. 2014), lower cost of debt, decreased risk-premiums due to lower bid-ask spreads and more accurate analyst forecasts (Dhaliwal et al. 2011). All these outcomes are highly desirable for management teams due to the positive effects these outcomes have on the bottom line.

Information about a company's sustainability performance is regarded as particularly asymmetric since it is difficult for stakeholders outside the company to gain credible information on relevant aspects vital for assessing how the company perform on the sustainability arenas (see Hahn and Kühnen 2013). The ambiguous nature of sustainability information adds to this complexity. Sustainability information is often criticized and questioned for being a PR invention rather than providing a true and fair view of a company (Frankental 2001). The limited credibility of sustainability may not only be caused by managements willingness to greenwash (bluewash and today even SDGwash) the company, it may also be due to management difficulties in "understanding," what sustainability is and how it should be measured, valued and assessed. Nevertheless, sustainability reporting receives criticism for its lack of value relevance and credibility. This impairs comparability and increases information asymmetry.

Previous literature even points to the fact that stock market actors claim that companies where the management team talk too much about sustainability without explaining its relevance to the value-creation process should be priced with a risk premium. Operationalization of sustainability information is challenging and results in a lack of reliable sustainability-related KPIs. Thus, there are substantial difficulties paired with trying to fit sustainability information into the analysts' excel sheets. The process of transforming our companies into more sustainable organizations will not slow down. Quite the opposite! Agenda 2030 and UN's Sustainability Development Goals (SDGs) clearly emphasize that sustainable businesses are the only way into the future.

This means that financial analysts need to understand, value and compare companies' sustainability performance. But how? How can they give and make sense of sustainability information? This is a great challenge! Until now, this problem has not been so acute and of need of urgent solutions. However, today it is a challenge that needs to be faced. Not the least due to the new EU directive (2014/95/EU) mandating the largest EU companies to disclose sustainability information. Furthermore, there is an increasing global sustainable investment market (Nilsson et al. 2014; Ramiah et al. 2016) that means that corporate-sustainability performance must be understood and assessed.

## Financial Analysts Play a Central Role in Sustainability Reporting

The previous sections have highlighted the central role financial analysts' play in intermediating information on the stock market. We have also discussed how sustainability information adds to a new type of smokescreen. The analysts are viewed as core users and intermediaries of sustainability information. In this section, we will further our understanding of both the financial analyst's work per se and the roles that two core types of analysts, buy-side and sell-side analysts, have in the sophisticated exchange of information. The above will be outlined with respect to sustainability information.

### The Financial Analyst's Work

Professional financial analysts need to be understood based on the context where they operate (Johansson 2007). In this case, as part of the value chain in the stock market, where they position themselves between the company and the investors and also as part of their own organizational setting, e.g. the investment bank. Researchers often consider analysts as proxies for investor beliefs in the stock market (Ivković and Jegadeesh 2004). Financial analysts are often appointed a critical role assuring information efficiency, an efficient allocation of finance, increased

liquidity and investor confidence in the stock market (Johansson 2007; Beyer et al. 2010; Clatworthy and Lee 2018). They intermediate information between publicly listed companies and investors in a context characterized of high information asymmetry, where a company's management team has more information and knowledge about the company than the typical investors have. Recent findings point to the analysts' proactive role in addition to the traditionally merely passive role as intermediaries. The proactive role implies gathering and providing information and analyses contributing with enhanced information to investors beyond the information intermediated by companies (Salzedo et al. 2018). Thus, they contribute with value-added services.

There are different types of financial analysts operating in the stock market, fulfilling different roles with respect to investors. This chapter specifically deals with two types of financial analysts, i.e. buy-side analysts and sell-side analysts. These are presented further below.

### Buy-Side Analysts—The In-House Generalist Group of Analysts

The buy-side analysts work for investment banks. They do not carry out the investments themselves, but they are responsible for internal investment advices in their *own* organizations, i.e. advices in-house to own fund managers (Brown et al. 2016). They support the fund managers with information, analyses and recommendations and decrease as such uncertainties and information asymmetry in fund managers' investment decision-making (see, e.g., Schipper 1991; Groysberg et al. 2011; Imam et al. 2008). Buy-side analysts are generalists, who covers a large number of companies and industries. In regard to use and communication of sustainability information, they collect, interpret and communicate value-added information to internal clients.

### Sell-Side Analysts—The External Specialist Group of Analysts

The sell-side analysts are specialists, covering a limited number of companies typically within one or a few industries. They work at investment banks' equity research departments where they produce external

recommendations and write analyst reports provided to their customers who are institutional investor organizations and brokerage houses. The sell-side analysts provide fund managers and buy-side analysts with information, analyses and recommendations and assist as such in decision-making. They primarily provide information to selected core customers, i.e. clients with a major part of their investments at the particular investment bank. They also produce written analyst reports with attached recommendations. Such analyst reports are available in different databases such as Investex and Bloomberg (Abhayawansa et al. 2017). The sell-side analysts' detailed coverage of listed companies and their industries decreases uncertainties and information asymmetry in the investors' decision-making process.

## The Cognitive Foundations: An Introduction to the Concepts

In this section, we outline the conceptual framework of cognitive frames particularly the concepts of sense-making, sense-giving and legitimacy in general. When we discuss the concepts, we do so without reference to sustainability information and financial analyst. The sustainability and analyst perspectives are added in the following sections.

### Sense-Making as a Concept

We apply a social-constructivist perspective in order to understand the underlying sense-making and sense-giving processes for use of sustainability information (Berger and Luckmann 1991). People in organizations try to clarify the situation by extracting and interpreting information in the organization, organize the information and try to make sense of what actually happens (Weick 1995; Weick et al. 2005). Sense-making is a social process where individuals construct their view of the world, a phenomenon, a situation, etc. They learn how to cognitively interpret the phenomenon or situation and how to behave and act in accordance with expectations (Weick 1979).

The sense-making process is considered as inherently social and discursive (Weick 1995; Weick et al. 2005). As such, "*Sensemaking is concerned with attempts to incorporate figural experiences into existing grounded institutional structures*" (Ifvarsson 2000, p. 102). The sense-making implies selectively organization and interpretation of information perceived as relevant for understanding the situation (Bean and Hamilton 2006). Tacit knowledge turns into more explicit knowledge throughout the sense-making processes (Weick 1995; Weick et al. 2005). Individuals react to the shaped environment at the same time as they also shape the environment. There are a dynamic creation and re-creation of meaning where individuals actively frame issues perceived as central while also reacting and modifying the view of, e.g., the situation at hand (cf. Gioia and Chittipeddi 1991; Weick 1993). It refers to "*the ongoing retrospective development of plausible images that rationalize what people are doing*" (Weick et al. 2005, p. 409). Nevertheless, we see this process as allowing for both retrospective (Weick 1995) and prospective processes (Gephart et al. 2010). The individuals' identity, and how individuals look at themselves, is central in the process of making sense (Weick et al. 2005). The sense-making process progresses through internal and external communication (Currie and Brown 2003).

The key themes of decision-making and change are common in the sense-making literature (Gioia and Thomas 1996; Rerup and Feldman 2011; Sonenshein 2010). Individuals face paradoxes in time when changes take place and managing change is thus much about managing these paradoxes (Nasim and Sushil 2011, p. 186). Sense-making allows for envision and revision of the meaning. There are also situations where individuals try to make sense of new, ambiguous and unclear situations that do not agree with expectations based on previous experience. There are tensions between the new and the old, involving needs of change causing uncertainty while a common way of dealing with uncertainty due to conflicting paradoxes is to strive towards order and stabilization and defending the old (Smith and Lewis 2011). As such, the sense-making process also touches on mechanisms of cognitive dissonance. When individuals perceive cognitive dissonance, they do not make sense of the situation or information at hand (Festinger 1962). Further, what is considered as cognitive dissonant is also considered as not legitimate.

## Sense-Giving as a Concept

Individuals actively construct the framing in sense-giving, focusing on what is central for communication to external stakeholders (Gioia and Chittipeddi 1991). Individuals aim to make an impact on other individuals' behaviour through the sense-giving in communication. "*'Sensegiving' is concerned with the process of attempting to influence the sensemaking and meaning construction of others toward a preferred redefinition of organizational reality*" (Gioia and Chittipeddi 1991, p. 442). While sense-making refers to the *cognition*, sense-giving refers to the *acting*. Norms and behaviour are central in communication when aiming to influence another party (Gioia and Chittipeddi 1991). "*Sensegiving-for-others*" involves disseminating of new understanding in front of the audience in order to influence their "sensemaking-for-self" (p. 444). The sense givers aim to influence the perceptions, attitudes and beliefs of others. The initial view may change throughout the sense-giving provided. In order to bond with others and influence others, social skills are therefore central in the sense-giving process (cf. Rosen and Kuehlwein 1996, p. 507).

Sense-giving allows for signalling and energizing while individuals as receivers of the sense-giving may be cynical about communication from influencers who mount them (Bommer et al. 2005; DeCelles et al. 2013). Sense-giving further enables development and nurturing of relations between individuals (Bean and Hamilton 2006). Regular interaction may develop a sense of shared identity that also may reinforce their common key values and the business opportunities. The commitment to the sense-giving organization may be due to such relationships potentially embarking new directions of enthusiasm rather than resistance (Awamleh and Gardner 1999). Sense-giving is provided in a cognitive frame, i.e. an interpretative scheme (Burtunek 1984) aimed to agree with the followers' interest, values and beliefs as well as organizational activities, goals and ideology (Walsh 1995, p. 281).

## Legitimacy as a Concept

The idea underlying legitimacy theory is that it is crucial for a company to be granted legitimacy in the form of a social contract often referred

to a social licence to operate (Dowling and Pfeffer 1975; Deegan 2002). Hooghiemstra (2000) argues that this implies that a company's success or even its survival in business society is dependent on the extent that the company is considered to operate within the norms of society (Brown and Deegan 1998). With ongoing shifts in norms and expectations, the threshold for what is being regarded as legitimate in society also changes. Legitimacy constitutes a critical driving source in organizational behaviour (Oliver 1991). We distinguish between two types of legitimacy, i.e. *cognitive legitimacy* and *social legitimacy*. The cognitive legitimacy refers to the people or organization's own legitimacy, i.e. if it is legitimate for the people to use and communicate sustainability information. It may for instance touche upon the peoples' awareness and knowledge about the phenomenon, uncertainties in interpretation and understanding of what it implies (Scott 1994, 1995; Zimmerman and Zeitz 2002). High cognitive legitimacy implies that knowledge is taken for granted, considered as useful and displayed in daily routines and activities, e.g. by professionals or organizations (Scott 2014).

Social legitimacy touches upon acceptance and support of social norms, e.g. on what is acceptable, appropriate or proper. In order to convince others to engage in and increase awareness and interest, there is a need to legitimate the new assumptions made based on the value of the socially constructed norms and beliefs (Suchman 1995). High social legitimacy implies that a social norm is accepted and supported by a particular group or society; it might be an accepted opinion, an accepted acting, etc.

## Analysts' Cognitive Frames in the Early 2000s

In this section and the following sect. "A Shift Towards Enhances Cognitive Legitimacy in Sense-Making and Sense-Giving", we continue to look into sense-making and sense-giving from the analyst's point of view but now explicitly with regard to sustainability information. We look into the analysts' cognitive frames also referred to as mental model, i.e. the cognitive meaningfulness and value attached to sustainability information (Schön and Rein 1994; Senge 1990). Much of the

change occurs due to shifts in norms and expectation in society paired with changes in sustainability-reporting regulations. We characterize the early 2000s as the *voluntary-reporting period* (sect. "Analysts' Cognitive Frames in the Early 2000s") and the latter half of the 2010s as the more *regulatory-reporting period* (sect. "A Shift Towards Enhances Cognitive Legitimacy in Sense-Making and Sense-Giving") when it comes to sustainability reporting. We further look into the analysts' legitimation and the concepts of cognitive and social legitimacy of sustainability *before* the changes from voluntary reporting to more mandatory sustainability reporting not the least with the new EU directive (2014/95/EU). In sect. "Analysts' Cognitive Frames in the Early 2000s" and "A Shift Towards Enhances Cognitive Legitimacy in Sense-Making and Sense-Giving", we further apply an internal organizational perspective on the analyst's work in line with Gioia and Thomas (1996). We combine this with an external perspective on sustainability communication and reporting in line with Morsing and Schultz (2006).

Thus, we now further conceptualize the cognitive frames of sustainability information in decision-making processes and communication processes from the analysts' point of view outlining the core sequences of sense-making and sense-giving. In order to understand the analyst's sense-making and sense-giving, we need to take a step back to management teams' cognitive processes of sense-making and sense-giving and how these in a later stage impact and influence the analysts' processes. Corporate information deriving from management teams is a central part of the analyst's work when interpreting, assessing and communicating companies' investment potential. As such, the management team's sequences of sense-making and sense-giving contextualize the analysts' sequences of sense-making and sense-giving.

Our framework enables analyses of the analysts' interplay with management teams, the analysts' adoption of sustainability information into their own work and their communication of value-added information with their clients, i.e. the investors. The framework enables outlining of the gradual development of sustainability reporting into a global reporting practice directly affecting the analysts' everyday work. In order to understand the shift in analysts' cognitive frames and challenges due to their views of sustainability information, we start from a historical

perspective a few years ago, then move further to the current state and start the conceptualization.

## Social Pressure on Companies to Report on Sustainability Information

In a first step, companies make sense of the sustainability information themselves in order to interpret and transform the information in order to disclose a true and fair view of the company stakeholders, here financial analysts. Despite the fact that the sustainability debate gained momentum over 30 years ago with the Brundtland report (UNWED 1987), the ambiguous nature of sustainability information still means difficulties for companies to understand how it should be reported in a relevant and credible manner. Reporting on sustainability information has until the fiscal year 2017, when the new EU directive (2014/95/EU) came into force, primarily been a voluntarily reporting practice engaged in by companies. Regulation of sustainability information is new, and norms of what to measure, how to measure, what to communicate or not all remain uncertain. Companies struggle with making sense of the sustainability information in the jungle of voluntary frameworks, guidelines and standards available (<IR> framework, UN Global Compact, Global Reporting Initiative (GRI) and UN's SDGs, ISO 26000). The scattered reporting landscape renders many questions for management teams to acknowledge. What does sustainability imply for us? What is material sustainability information? To whom is it material? How can we understand and assess sustainability performance? How can sustainability information be connected to traditional financial corporate information? What consequences might be expected due to how sustainability information is reported, e.g. how does it affect the analysts' work and their views and valuation of the company.

A major shift took place for the companies in the early 2000s where expectations on companies to report on sustainability information increased in the aftermath of the many corporate scandals. This meant that the norms, values and expectations of what were considered legitimate (Dowling and Pfeffer 1975; Deegan 2002) in a sustainable, ethical

and responsible context changed in society. This forced companies to develop their business conducts in a more responsible and sustainable way. To show their achievements and to be granted legitimacy, companies started to voluntarily engage in developing their sustainability-reporting practice (see Arvidsson 2010, 2011, 2012). It was at this point in time challenging for management teams to both make sense of sustainability information themselves and to give sense to this information to financial analysts. This implies that the management teams were not conscious, or at least unsure of what signals their sustainability reporting was sending to the financial analysts.

## Cognitive Dissonance Due to a Lack of Cognitive Legitimacy

During the first decade of this century, when companies started to increase the focus on sustainability in their corporate reports, most analysts did not find this type of information neither relevant nor credible (Arvidsson 2014). Although management teams tried to convince the analysts and also their clients, i.e. the investors, of its value relevance, they were of the opinion that sustainability information was something that companies only provided for legitimacy reasons not for its relevance for corporate valuation. They did not seem to see a clear link between sustainability information and the corporate value-creation process. Nor did they seem to understand how sustainability fitted into business models, organizational routines and processes (Arvidsson 2014).[2] This led to scepticism towards the relevance of sustainability reporting and it was often considered a "greenwashing" and "bluewashing" reporting practice. Thus, the analysts were reluctant to make sense of the information and the information was not perceived as cognitive legitimate by the analysts. Analysts stated (Arvidsson 2014, p. 217):

> Management teams go on and on and on about their CSR [sustainability] activities.

> Neither me or my colleagues require CSR [sustainability] information.

Here, a situation of cognitive dissonance appears where the analysts kept to the well-known cognitive frame of reference of corporate *financial* information, implying a cognitive denial of sustainability information. The cognitive dissonance served as a gatekeeper for sustainability information and, therefore, hindered the analysts' sense-making of this information (cf. Festinger 1962). Analysts also stated (Arvidsson 2014, p. 217):

> The management teams talk more about CSR [sustainability] – but we do not listen.

This indicates that financial analysts reflect on the value of sustainability information and appear to find it of limited relevance for future value creation and, thus, not material in their work of interpreting, assessing and communicating corporate performance. As a consequence, they take at this stage a passive approach towards sustainability information, meaning that it is not actively included in their investment advices. This standpoint is further reflected in the following quotes (Arvidsson 2014, p. 217):

> The interest in CSR [sustainability] information from us financial analysts are and has always been extremely limited.

> The CSR [sustainability] information makes no difference and is of no interest to a financial analyst.

> Complete mumbo jumbo!

Here, we clearly see that the analysts due to the perceived lack of value did not cognitively legitimate sustainability information. They appear reluctant to make sense of the information. The cognitive frame of reference which still was centred around corporate *financial* information promotes this reluctant and passive behaviour. Probably, this was also reinforced by the fact that they regarded it challenging to understand sustainability information and that this prevented them from acting on this information (cf. Gioia et al. 1994). Difficulties in transforming the "soft" sustainability information into more "hard" financial information served as a barrier in the financial analysts' sense-making process.

The financial analysts appear to find sustainability information ambiguous and difficult to translate into monetary terms applicable in their Excel sheet context (Arvidsson 2014). The scattered reporting landscape resulted in an abundance of different ways to report on sustainability performance. This impaired the comparability of sustainability performance between companies, periods and industries. Considering the analysts' mission to generate profits for their investment bank, a consequence of the difficulties and ambiguity surrounding sustainability information appears to have made them hesitant to spend resources on actively engaging in the process of transforming sustainability information into more familiar type of information. Instead, they focused their sense-making efforts on traditional financial information, which they considered to be more meaningful when interpreting and assessing corporate performance and value.

At this time, there was a notion that companies primarily reported on information related to positive sustainability issues rather than negative (Emeseh och Songi 2014). However, the analysts appeared to be more interested in making sense of information related to incidents of *negative* sustainability character, e.g. pollution, use of child labour, unethical business conduct, violation against human rights and corruption. Already here, a gradual shift can be identified where analysts started to include sustainability information as part of their assessment of companies' risk profiles (Arvidsson 2014). The following quote (Arvidsson 2014, p. 218) reveals that a distinction is made between value creation and value destruction.

> CSR [sustainability] has more to do with avoidance of value destruction than value creation.

> CSR [sustainability] does not create value per se. It could, if handled correctly, assist in avoiding value destruction due to being caught in engaging in bad activities.

In this section, we outline how sustainability information in the first decade of the twentieth century affected the analysts' sense-making and sense-giving processes (Weick et al. 2005). The sustainability information is neither social legitimated nor cognitive legitimated by the analysts. Analysts' are unable to make sense of the ambiguous sustainability information; the information is not cognitively legitimated. The information is not

social legitimate; it is not requested by the analysts' clients, not considered as value adding, not generating a pay-off and considered as purely a cost for the investment bank. The analysts face cognitive dissonance (Festinger 1962). They are unwilling to engage in sense-making activities and do not actively engage in sense-giving activities in front of clients.

## A Shift Towards Enhances Cognitive Legitimacy in Sense-Making and Sense-Giving

We now look into more regulatory-reporting practice regarding sustainability reporting that characterize the latter part of 2010s. Here, we see a change in analysts' use and value attached to sustainability information, which we argue is caused by a shift in analysts' cognitive frames (Schön and Rein 1994; Senge 1990). Much of the change occurs due to shifts in norms and expectation in society paired with changes in sustainability-reporting regulations. On the one hand, there is now starting to be a societal pressure on management teams to run their business in a more sustainable manner and increase the quality of how they report on their sustainability performance. On the other hand, there is also a societal pressure on institutional investors to make sound investment decisions incorporating sustainability aspects. This societal pressure is paired with a changing reporting landscape towards more regulatory-reporting practices. We further look into the analysts' legitimation and the concepts of cognitive and social legitimacy of sustainability *after* the changes from voluntary reporting to more mandatory sustainability reporting not the least with the new EU directive (2014/95/EU). We continue to outline the analysts' core sequences of sense-making and sense-giving moving to the current state in the post-regulation period.

### Increased Societal Pressure for More Sustainability Focus

The second decade of the twentieth century has been characterized by an increased societal pressure on companies to enhance the quality, relevance, credibility and comparability of sustainability information. Today, with Agenda 2030 and UN's SDGs we can conclude that

sustainability is a topic high up on the agendas in politics, business society and academia. National and international regulations concerning, e.g. inclusion of sustainable perspectives on investment valuations, emissions, disclosure rules, tax transparency, compliance and anti-corruption are continuously taking a step forward. This imposes pressure on companies to provide structured and relevant information on these issues in their sustainability reporting. It also assists companies in sorting out what is relevant and material. A change is now taking place, which relates to sustainability information becoming more regulated and not only a voluntary-reporting practice. From the fiscal year 2017, the largest EU companies are mandated to disclose sustainability information in accordance with the EU directive (2014/95/EU).

The stakeholders harshly question and dislike companies that do not provide sustainability information or if they do not act in accordance with norms, values and expectations. Recently, HM was criticized for a racial tone in a sweater advertisement and for high risks of using child labour in their production (SvD 2018). Thus, sustainability issues have stepwise come to have an impact on share prices and, thus, corporate valuation particularly via news scandals (Aerts et al. 2008). In addition, Zhou et al. (2017) find that sustainability reporting by decrease the information asymmetry and reducing the information risk also decrease errors in analysts forecast and forecast dispersion.

There has been an increased pressure not only on management teams to engage in sustainability reporting but also on institutional investors to act and invest in accordance with sustainability criterion. The pressure on institutional investors primarily come from non-profit organizations (NPOs) and governments (Cornett et al. 2016). This is also illustrated through the following quotation by one investor in the study by Essland and Olausson (2018, pp. 20–21)[3]:

> It all started with the churches, and this was many years ago, they did not want their money to be invested in unethical industries such as pornography or tobacco. Later the municipalities started making the same requests due to political forces, and nowadays I do not believe we have a single institutional customer who do not demand certain restrictions in the investment universe.

The amount of capital invested in sustainable funds has extensively increased in recent years (Nilsson et al. 2014) and such investments expect to continue to increase in both relevance and numbers (Ramiah et al. 2016). Pension funds classified as environmental or ethical had over a period of five years shown lower fees and higher return on investments compared to other funds (Sievänen et al. 2013). Thus, sustainability has become a selling argument for investment funds. Sustainability information has thereby become value-added information and a natural part of the analysts' investment advices to clients.

## Management and Institutional Investors Forced to Make Sense and Give Sense

Today, companies are forced by investors and analysts to become more transparent both in their communication of sustainability information and in acting in accordance with the norms of being a sustainable business. As such, management teams need to frame themselves as social legitimate both in reporting and in acting (Massaro et al. 2018). Company reports have traditionally focused merely on historical financial information while mandatory regulation now forces companies to integrate sustainability information, information capturing both the history and the future. Sustainability information has become central for companies' future performance and value (Eccles et al. 2014).

Management teams actively interpret, assess and communicate sustainability information, i.e. make sense and give sense to sustainability information. Institutional investors are now also pressured by actors such as NPOs and government to make sustainable investments (Cornett et al. 2016). Hence, they request sustainability information in order to signal their social legitimacy by investing in sustainable companies. For this, they need to make sense of and to give sense of sustainable investments. This is also illustrated through the following quotation by one investor in the study by Essland and Olausson (2018, p. 21):

> We have seen a tremendous increase in pressure from the surroundings when it comes to our sustainability screening and investment decisions. I believe

> that this pressure will continue, maybe even increase and that sustainable investments will be a hygiene factor rather than a differentiation factor.

There are a number of ongoing initiatives for instance an engagement programme by banks in Europe and USA, ShareAction, where small shareholders and institutional investors work together for taking an active standpoint and impact on the climate change (Share Action 2017: https://shareaction.org/in-the-news/boston-common-and-share-action-working-on-transatlantic-bank-engagement-on-climate-change/):

> Investors can protect themselves from stranded assets but they remain exposed to macro high-carbon risks. Banks are uniquely placed to influence actors across the emissions chain. By financing high-carbon, banks can contribute to temperature rises. Engaging with banks could avoid portfolio-wide exposure to climate risk.

The discussion above outlines the strategic change taking place where a vigorous practice for sustainability reporting is developing among companies and investors. This also affects the analysts' work with providing value-added information and, hence, also on the analysts cognitive frames regarding meaningfulness and values of sustainability information.

## Analysts' Cognitive Frames: Sustainability Becomes Cognitive Legitimated

Operating within the norms of society is central for the analysts (cf. Brown and Deegan 1998) in order to assure for social legitimacy. There is an ongoing strategic change that takes place for analysts, transforming sustainability information into cognitive legitimate information. Analysts need transparency to surround corporate-sustainability information in order to evaluate potential and to assure for relevant and credible value-added advices to clients (Newell and Paterson 2009). In this process of starting to include a new type of information, i.e. sustainability information, there is a questioning of traditional norms and transformation into new norms values and believes (Suddaby and Greenwood 2005; cf. Gioia and Chittipeddi 1991).

A number of critical factors are involved in the process of decreasing the smokescreen of sustainability information. When sustainability reporting becomes more regulated, e.g. through the new EU directive (2014/95/EU), the sustainability information provided by companies opens up for less problems for analysts related to interpretation and valuation. This is due to increased transparency and also enhanced comparability. The financial analysts take a role as "meaning-makers" and want as such to influence their clients in order to achieve their organizational goals, i.e. generating businesses for the investment bank and for institutional investors to make beneficial investments. The analysts have an active role as facilitators, expected to have adequate competences to interpret, assess and provide relevant and reliable investment advices based on a mix of traditional financial information and sustainability information. When these prerequisites are achieved, analysts are ready to take an active part in the sense-making and sense-giving of sustainability information. The cognitive dissonance is no longer the problem hindering an active interpretation, assessment and communication. Through sense-giving, analysts influence and assist investors to better identify and understand investment opportunities.

However, empirical evidence reveals that not even mandatory requirements appear to be a quick fix when it comes to the alleged shortcomings with sustainability information in corporate reports. The informational quality confirms to be low even in countries with mandatory requirements on sustainability reporting (Chauvey et al. 2015; Larrinaga et al. 2002). This also received attention at the recent SUBREA conference (Arvidsson 2018), where it was highlighted that financial analysts *still* find it challenging to work with sustainability information. One critical barrier is the analysts' inability to make sense of this kind of new type of information (Abhayawansa et al. 2018). Efficient measurement techniques relevant for sustainability information are particularly requested by the analysts in order to deal with the ambiguity (Perez and Sanchez 2009). This is also illustrated through the following quotations from the study by Essland and Olausson (2018):

> I can measure a whole bunch of stuff, for example the 2 emissions from a company that manufactures cluster bombs, but that would not be that relevant, right? This is the hard part. (p. 23)

> Take the automotive industry, it is very problematic to evaluate regulatory risks. What will happen with diesel cars? Will there be tax reliefs for electric cars? We are not used to working with these potential changes in regulations. (p. 29)

This implies a pressure on analysts to engage in and actively integrate sustainability information provided through corporate reports despite the ambiguous nature of the information. The analysts' ability to interpret and assess sustainability information and hence their own sense-making processes become critical in order to provide value-added information and investment advice to clients. It is now to a greater extent *expected* of analysts to be able to provide this.

The relationships between management teams, financial analysts and investors become central in the sense-making and sense-giving processes of ambiguous sustainability information. Uncertainties are expected to be dealt with through the dual exchange of information between management teams, financial analysts and investors. Management teams play a central role in the analysts' sense-making efforts by actively engaging in sense-giving enabling analysts to provide relevant investment advices to their clients, i.e. the investors. As such, analysts' sense-making and sense-giving processes are closely intervened with sense-making and sense-giving by the management team. This also expects to be the case for the exchange between analysts and investors. According to a study by Abhayawansa et al. (2018), the main and preferred methods for analysts' gathering of information are through personal meetings with company management and conference calls. Sense-giving entails communication with management teams and clients via meetings and other types of direct and indirect communication and allows for interactively sense-making of corporate values. Direct contacts improve the potential for analysts' sense-making, especially when ambiguous information is at focus and, thereby, enables analysts to provide value-added investment advices to the investors (Johansson 2004, 2007). Although they rely on direct contacts, the analysts highlight the need for them to independently make sense of sustainability information. The independence does not exclude them from incorporating information from various corporate representatives with

different types of informational input needed for them to make efficient investment advices. This is illustrated by the quotation by one analyst in the study by Abhayawansa et al. (2018, p. 24).[4]

> You can't collect information on that [i.e., strategic focus and future orientation]. You develop a view. Strategic focus is a means. You listen to what the CEO says - that's what's on the surface of it. You want to dig deeper than that. You want to speak to the guys who are technically involved in the company - not at the management level.

The analysts' sense-making and sense-giving processes appear to be iterative, sequential and mutual inclusive in nature involving a giving and taking between companies—analysts and investors (cf. Gioia and Chittipeddi 1991). The sequences involve the key actors *understanding* of the situation, i.e. the corporate value or potential, through sense-making and then *affecting* the investors' investments by *sense-giving* through relevant and credible investment advices. The analysts continuously interact with management teams and investors. They make sense of the situation; they revise their meaning and try to give sense of the information to investors by envisioning and energizing their standpoint. The analysts "sell" their investment advice, i.e. their view of a company's potential as an investment. These investment advices represent sense-giving while at the same time the analysts try to make sense *themselves* of the sustainability information at hand. The cycles involve as such both *cognition* and *action*.

Direct contacts may also allow for development of a *shared* framework of what is central when interpreting and assessing sustainability information. The sense-giving encapsulates social skills in the communication of the investment advices.

In this section, we have outlined how sustainability information in the latter part of the second decade of the twentieth century affected the analysts' sense-making and sense-giving processes (Weick et al. 2005). Sustainability information is now beginning to be socially legitimate and requested by the analysts' clients, i.e. investors. However, the complexity of the situation remains. This type of information is still not considered as cognitive legitimate due to the ambiguous nature, which

renders difficulties for the sense-making and sense-giving processes. The information is not yet internalized into the analysts' cognitive frames, i.e. not taken for granted and integrated into the analysts' daily work (Scott 1994). Although analysts are still unable to make (perfect) sense of the ambiguous sustainability information, they are now willing to engage in sense-making activities due to the pressure of social legitimacy, i.e. investors expect this to be included in the analysts' value-added information. There appears to be a situation, which we refer to as a partial cognitive dissonance. Engaging in sense-making does no longer solely imply non-profit generating work, i.e. simple waste of resources. Engagement also generates pay-off since analysts' clients consider the information as value relevant and adding additional value to their investment decisions. In order to provide value-added information, analysts now need to be able to interpret both traditional financial information and sustainability information for making sense of what constitutes high potential investments (cf. Malmström et al. 2015). They are now expected to actively engage in *giving* sense of sustainability information to their clients. We have seen that the analysts' relationships with management teams and investors are central in their continuous sense-making and sense-giving of sustainability information. Efficient relationships enable analysts to decrease the perceived ambiguity and stepwise develop commonly accepted norms of sustainability information together with companies and clients (Scott 2014; Zimmerman and Zeitz 2002).

## Cognitive Foundations and a Promising Future Ahead

In this chapter, adopted a sense-making and sense-giving perspective on how analysts work as information intermediaries and how an increased focus on sustainability information in corporate reports has affected their work. In particular, we wanted to highlight the challenges in sense-making and sense-giving to gain a better understanding of their interpretation, assessment and communication of sustainability information to their clients, i.e. the investors. This chapter problematizes

the challenges due to *social legitimation* (i.e. investors' request of sustainability information) and *cognitive legitimation* (analysts' ability to understand the ambiguous sustainability information) and as a result, the hurdles of cognitive dissonance make analysts hesitant towards considering sustainability information in their day-to-day work. We develop a new perspective drawing on analysts' cognitive foundation underlying the smokescreen of sustainability information.

The discussion outlines changes in the analysts' cognitive frames from the first decade of the twentieth century to the second decade of the twentieth century. We argue that the first part of 2000s was characterized by cognitive dissonance due to both a low social legitimacy (sustainability was not yet requested by the investors to be attended to) and a low cognitive legitimacy (sustainability was regarded too ambiguous to be relevant for being considered in a valuation context). In the latter part of 2010s, we argue that there is only a partial cognitive dissonance. Now, sustainability information is beginning to be socially legitimate and requested by investors. However, the complexity of the situation remains. This type of information is still not considered as cognitive legitimate due to the ambiguous nature, which renders difficulties for the analysts' sense-making and sense-giving processes.

We can conclude that sustainability is largely about people, about the key actors in the stock market and their ability and willingness to make sense and give sense of sustainability information and to act in accordance with sustainability criterion. It is much about legitimate behaviour and accomplishes changes in values, norms and behaviour. Both cognition and action play vital roles in this process. In sum, we see a promising future ahead where sustainability information gradually is becoming (becomes?) more relevant, credible and comparable. The process of decreasing its ambiguous nature will result higher cognitive legitimacy of sustainability information. This will promote the integration of sustainability information in the analysts' work of providing efficient investment advices to investors. The findings have implications not the least in the ongoing quest of developing frameworks, standards and legislation (e.g. the EU directive (2014/EU/95)), that opt for improving the relevance, credibility and comparability of sustainability information. We finally conclude that:

> In truth, the core nature of investment and return is not a trade-off between social and financial interest but rather the pursuit of an embedded value proposition composed of both. (Emerson 2003, p. 37)

## Notes

1. R*eading tip*: Summa de arithmetica, geometria, proportioni et proportionalita by Luca Pacioli from 1492.
2. The semi-structured interviews in Arvidsson (2014) were conducted in 2010 with 17 financial analysts working at international investment banks. In this chapter, CSR is used as a proxy for sustainability.
3. The semi-structured interviews in Essland and Olausson (2018) were conducted in 2018 with 19 key actors in the stock market, primarily working at international investment banks.
4. The semi-structured interviews in Abhayawansa et al. (2018) were conducted with 23 analysts in the stock market, primarily working at international investment banks.

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