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Does Sustainability Reporting Improve SME Access to Finance? Evidence From NBS Bank and PolyMed Sacco, Blantyre, Malawi

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ABSTRACT

The external financing of small and medium enterprises (SMEs) in emerging economies is a persistent challenge, in part due to a lack of information for lenders regarding the operations, governance and long-term risks of the SMEs. This study investigates the hypothesis of the impact of sustainability reporting on SMEs access to finance in Blantyre, Malawi based on the evidence given by NBS Bank and PolyMed SACCO. A convergent parallel mixed-methods design was used, which involved surveying 156 SMEs, and also using qualitative interviews with financial-institution managers and loan officers. A version of an ESG Disclosure Index derived from existing disclosures was used to measure sustainability disclosure. Data were analyzed using descriptive statistics and Pearson correlation analysis for quantitative data and thematic analysis for qualitative data. The quantitative results indicated that the ESG related report has no statistically significant relationship with access to finance. Qualitative evidence indicates, however, that sustainability information may help to improve transparency and lenders' understanding of business practices and management quality. The results indicate that formalization of sustainability reporting is still not very developed and, therefore, limited in usefulness for SME lending. There is a need for simplified reporting guidance on ESG, building capacity and proportional integration of sustainability information into SME finance, the study recommends.

Keywords: Sustainability reporting, SME financing, ESG disclosure, Access to finance, Malawi, Emerging economies

INTRODUCTION

Small and medium enterprises (SMEs) are common factors in the process of economic development in terms of employment creation, innovation, income generation and poverty reduction [1] . SMEs are the major part of business enterprises and important in supporting the economic growth and livelihood improvement in emerging economies. Many small and medium enterprises (SMEs) face significant difficulties when it comes to accessing formal finance although they are economically significant. Access to credit is limited and impacts the ability to expand the business, investment opportunities, and sustainability of long-term business operations [2]. .

While the private sector is largely made up of SMEs in Malawi, it is not sufficiently served financially. Numerous business owners are not registered, do not keep good books and do not have sufficient collateral or meet traditional lending criteria. As a result, financial institutions still heavily use the conventional credit assessment metrics such as the audited financial statements, historical profitability, collateral availability and credit history in assessing loan applications [3] .These criteria are designed to minimize the risk of lending but often have detrimental effects on otherwise sound SMEs who may not have adequate paperwork and assets.

One of the major difficulties that lie behind the SME financing is the information asymmetry of the borrowers and the lenders. Information asymmetry theory states that lenders may not always have complete information about the creditworthiness or the financial condition, management ability and risk profile of the borrowers firms, which adds to the uncertainty in the credit assessment process [1]. Consequently, lenders employ screening processes which often deny external funding to SMEs. While financial information continues to be a key factor in lending decisions, more and more emphasis has been put on non-financial information to be considered in making lending decisions as a measure of organizational quality and risk.

Sustainability reporting has become a source of non-financial information that is significant. Organizations disclose information about their environmental, social and governance (ESG) practices, which help communicate how they are managing sustainability-related risks, responsibilities and value creation in the long term [4] . Today, sustainable finance is gaining popularity globally and is putting an increasing pressure on SMEs to demonstrate responsible business practices, although it has previously been a focus for big companies.

A signaling theory further discusses how sustainability reporting is related to access to finance. Disclosure of sustainability information voluntarily can be interpreted as good governance and management practices and can result in reduced operational risks, which could lead to improved lender confidence and decreased uncertainty in the lending process [2]. Thus, sustainability reporting can be used to supplement financial information and offer further information about the sustainability resilience and sustainability management of an enterprise.

Although there is a growing interest in sustainable finance around the world, empirical studies on the link between sustainable finance and finance availability for SMEs are still lacking, especially in developing economies. Most of the existing research has been conducted in large firms in developed countries where sustainability reporting frameworks are fairly developed. Little is known about whether the disclosure of ESG information affects lending decisions in SME financing in emerging financial systems like Malawi. In addition, there is a wide variation in financial institutions' methods of financial lending. While commercial banks generally focus on formal documents, performance and quantitative risk assessment, Savings and Credit Cooperative Organizations (SACCOs) tend to pay more attention to member relations, savings behavior and community based information [5] . It is, therefore, important to research and practice if these institutional differences affect the relevance of sustainability reporting.

In light of this, this study aims at finding out the impact of sustainability reporting on the access to finance for SMEs in Blantyre, Malawi, based on the findings from NBS bank and PolyMed SACCO. In particular, the research investigates the extent and nature of sustainability reporting of SMEs, the link between ESG disclosure and financing results, and the heath banks' perspective on sustainability information in credit assessments. This study fills the empirical knowledge gap in the context of Africa and offers insights for SMEs, financial institutions, and policymakers to enhance financial inclusion by improving information disclosure.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Sustainability Reporting and SME Access to Finance

Sustainability reporting has grown from being a voluntary corporate communication activity to a more prominent tool for communication of an organization's environmental, social and governance (ESG) performance to its stakeholders. Sustainability reporting has historically been linked to big multinational companies, but in recent years, it has come to be more relevant for small and medium enterprises (SMEs), due to the greater relevance that governments, investors, customers, regulators and financial institutions give to responsible business and sustainable development [4]. While SMEs may not be able to create a detailed sustainability report, many undertake business sustainability activities relating to the environment, employee wellbeing, ethical governance and engagement with their communities that can be expressed through a simplified sustainability disclosure [6].

In addition to the regulatory aspect, sustainability reporting builds organization transparency, accountability and stakeholder trust. Firms are submitting extra data regarding their ESG-related activities voluntarily, which indicates management quality, governance practices, and a long-term strategic perspective, and decreases uncertainty among external parties. The disclosures are especially important for SMEs, as they are often constrained in their ability to access credit because they lack information in the public records, have less robust governance, and have shorter credit history [1] . With this in mind, sustainability reporting can be used as an adjunct to financial information, offering lender information on an enterprise's potential long-term viability and risk.

The increasing relevance of sustainable finance has further enhanced the relevance of ESG information in the credit assessment. Environmental risk, failure of governance, and social issues are growingly being recognized as potential factors that could impact borrowers' financial performance and ability to repay the loans [7]. Although the integration of ESG is more advanced in developed economies, financial institutions in developing economies are increasingly integrating non-financial information in their lending decision as awareness about sustainable finance is growing.

Even with this progress, only a fraction of SMEs, especially in Sub-Saharan Africa, report formally on sustainability. Adoption is still constrained by resource constraints, limited technical expertise, low awareness of ESG reporting frameworks and lack of mandatory requirements [5]. This means that many SMEs carry out sustainability related activities, but do not systematically record or communicate these to external stakeholders. The disconnect in sustainability practices and disclosure could diminish the value of ESG information in terms of the lending process.

Information Asymmetry Theory

The Theory provides one of the principle explanations for financing challenges experienced by SMEs. Akerlof's information asymmetry theory explains that markets may fail to allocate resources efficiently when one party possesses more information than the other [8]. In a credit market, business owners typically have more knowledge about the condition of their business, the risks that it faces, and the future prospects of their business than would be the case for anyone considering lending to the business. This imbalance leads to uncertainty in the credit process making lending more risky [8] .

To minimize this uncertainty, lenders may impose more stringent screening criteria, such as requiring, for instance, more collateral, a higher interest rate, a smaller loan size, or a rejection of the loan application itself [9]. These practices are disproportionate to SMEs, who will tend to have less formal financial documentation and shorter credit histories than larger businesses.

Some extent, information asymmetry can be addressed by sustainability reporting, as lenders may obtain other evidence of ethical business conduct, environmental responsibility, good governance and risk management practices. These disclosures support traditional financial statements and provide a more comprehensive measure of organizational quality. But the impact of sustainability reporting to information asymmetry, in the end, will rely on the capacity and willingness of financial institutions to acknowledge and integrate ESG information when assessing loans. The impact of sustainability reporting on lending practices is likely to be limited where traditional financial practices are still the primary drivers.

Signaling Theory

Signaling theory complements information asymmetry theory as it is a theory that seeks to explain the willingness of organizations to provide information to make them stand out in markets where information is imperfect [10]. Incentive therefore exists for firms with favorable characteristics to make credible signals to lower uncertainty for external stakeholders and increase perceptions of the quality of the firm.

In the SME financing landscape, sustainability reporting could be such a signal. Environmental stewardship, responsible labor practices, sound governance and ethical business practices can be disclosed voluntarily and can suggest effective management, sound internal control and reduced operational risk. These attributes could build lenders confidence in the borrower's ability to fulfill financial commitments and continue to perform in the future.

Signals must be credible, observable, and hard to replicate, though, to influence decision-making. In order to be meaningful, sustainability reporting requires not only a commitment by the organization but also strong reporting practices, enhancing the credibility of what is disclosed. However, even though sustainability reporting is a signal of sustainability, it is not likely to have a significant impact on lending results in practice, where financial institutions attach little importance to ESG information in their credit assessment processes.

Stakeholder Theory

The stakeholder theory is that companies achieve sustainable value when they take into consideration the interests of various stakeholder groups rather than just shareholders. The stakeholders that impact the performance and future of an organization include employees, customers, suppliers, investors, regulators, governments, local communities and financial institutions.

Reporting on sustainability is a key tool by which organizations can be held accountable to these stakeholders. Environmental, Social and Governance (ESG) reporting provides companies with a consistent way to share their ESG performance, signaling their dedication to making responsible business choices, transparency, and ethical oversight. These disclosures serve to enhance the legitimacy of the organization, build stakeholder trust, and help to establish relationships.

Positive relationships with financial institutions are a key stakeholder goal for SMEs. While financial performance will remain the driving force behind credit assessment, sustainability disclosures can give lenders further confidence in management quality, governance, ethics and resilience of the organization. In the stakeholder theory view, sustainability reporting is thus seen to build the organization's legitimacy and trust among stakeholders, leading to an indirect route on which SMEs could extend external funding opportunities.

METHODOLOGY

Research design

The study used the convergent parallel mixed methods design that entails collecting quantitative and qualitative data simultaneously, analyzing them separately, and then combining them for results interpretation [11].The mixed methods approach was deemed suitable as a part of the study involved identifying if there is a significant influence of sustainability reporting on SMEs' access to finance and also investigating the perception of financial institutions in the context of credit assessment. A multi-sourced combination of quantitative and qualitative evidence thus allowed for a fuller understanding of the phenomenon than could either type of evidence alone.

The quantitative part looked at the sustainability reporting-finance nexus based on survey data of SMEs. The qualitative analysis involved conducting semi-structured interviews with NBS Bank and PolyMed SACO managers and loan officers, which were used to gain context on institutional lending practices and the use of sustainability information in the loan evaluation process.

Study Area

The study was carried out in Blantyre District, the main commercial and industrial Centre of Malawi. Apart from the commercial banks, Savings and Credit Cooperative Organizations (SACCOs) and other financial institutions, Blantyre is a high concentration of SMEs in the retail, manufacturing and service sector. Thus, the district offered a suitable context in which to investigate the connection between sustainability reporting and access to finance for SMEs.

To determine the population and sampling.

The target population were SMEs in Blantyre District and staff of financial institutions in the decision making process.

The quantitative component consisted of 156 SMEs sampled from an estimated population of around 150,000 SMEs with the aid of the sample size formula suggested by Yamane (1967). In order to make sure that good representation is achieved, SMEs have been chosen from the retail, manufacturing and service sectors.

The qualitative component made use of purposive sampling technique, which yielded eight key informants, representing managers and loan officers of the two organizations NBS Bank and PolyMed SACCO. The participants were chosen because they were directly involved in the assessment of SME loan applications and were knowledgeable about the practices of institutional lending.

Data Collection

A structured questionnaire was used to gather quantitative data from SME owners/managers. The questionnaire gathered the data regarding the characteristics of the firm, sustainability reporting, financing, and business performance. A structured checklist of environmental, social and governance (ESG) disclosure questions adapted from the Global Reporting Initiative (GRI) Standards [4] was used to measure sustainability reporting.

Data gathered were qualitative, consisting of interviews with managers and loan officers of the financial institutions involved, using semi-structured format. The questions addressed in the interview guide included the criteria considered for lending, the perceptions of sustainability reporting, challenges to financing SMEs and the importance of non-financial information in the credit assessment process. These interviews gave contextual explanations which complemented the quantitative findings.

Measurement of Variables

Independent Variable: Sustainability reporting was identified as the independent variable which was operationalized through an ESG Disclosure Index based on the Global Reporting Initiative (GRI) Standards and adapted to address the reporting capacity of SMEs. The index measured disclosure in three areas: Environmental disclosure (waste management, resource efficiency, pollution prevention and environmental awareness campaigns).Social disclosure, such as employee welfare, occupational health and safety, customer responsibility and community engagement. Governance disclosures (ownership, financial transparency, ethical business conduct and internal control practices).All SME disclosures were evaluated by marking each disclosure item to indicate if it was part of the SME's disclosures. Individual scores were combined and standardized into a score on a standardized ESG Disclosure Index ranging from 0 to 100 with higher scores indicating higher degrees of sustainability disclosure.

Dependent Variable: Access to finance was the dependent variable and was assessed by four indicators:

Whether a loan has been approved (binary: 1 = approved, 0 = not approved);

- The amount of loans obtained (Loan size);
- The interest rate that will be paid on the loan; and
- Collateral requirement (binary: required = 1, not required = 0).

Control Variables

To reduce omitted variable bias, the following characteristics of firms were incorporated into the regression models that are typically associated with SME financing outcomes:

- Firm age;
- Firm size;
- Sector of operation;
- Profitability; and
- Collateral availability.

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These factors have been consistently found in previous research to be relevant for SMEs access to finance [12].

Data Analysis

The analyses of quantitative data were carried out on IBM SPSS Statistics software. Firm characteristics and sustainability reporting practices were summarized using descriptive statistics such as frequencies, percentages, means, and standard deviations. IBM SPSS Statistics was used to analyze the quantitative data. The characteristics of the SMEs and their sustainability reporting were summarized using descriptive statistics, such as frequencies, percentages, means and standard deviations. Pearson correlation analysis was then used to explore the direction and strength of the relationship between ESG related reporting variables and access to finance outcomes. Significant difference was considered at the 5% level of significance. Because the data are cross-sectional, conclusions are drawn in terms of associations and not cause and effect.

Thematic analysis was then used to analyses the qualitative interview data, which was done in six steps outlined by Braun and Clarke [13]. The interview transcripts were read multiple times to familiarize one and then meaningful statements were coded. These codes were then organized into larger themes: Sustainability reporting, financing constraints, lending criteria, and institutional perceptions of sustainability information. The qualitative findings were then analyzed with quantitative findings to give an in-depth interpretation of the research findings [13] .

Validity, Reliability, and Ethical Considerations

The ESG Disclosure Index was created based on a checklist that was adapted from the Global Reporting Initiative (GRI) Standards and relevant literature, and was structured to consider the reporting capabilities and operating environment of SMEs. Environmental, social and governance disclosures were included in the index, such as waste management, resource efficiency and pollution prevention, employee welfare, occupational health and safety, as well as customer responsibility and community engagement, and ownership, financial transparency, ethical business conduct and internal control. All disclosure items were coded for the presence of the information related to sustainability in the SME disclosure. The item scores for all three of the E, S, and G factors were then averaged across the three and normalized to create an ESG Disclosure Index ranging from 0 to 100, with higher scores representing more sustainability disclosure. Content validity was achieved by adjusting items to reflect existing sustainability-reporting frameworks and literature. A pilot study was also carried out prior to the main survey to evaluate the clarity, relevance and consistency of the research instrument, and some minor changes were made to the questions to enhance the language and sequence during this process. To evaluate the reliability and construct validity of the ESG Disclosure Index, principal component analysis (PCA) and internal consistency measures were used. The retained indicators were associated with their respective factors with PCA result loadings that ranged from 0.687 to 0.898, which means that the retained indicators had meaningful associations with their respective factors. The internal consistency was measured by Cronbach's alpha for the extracted components, with Cronbach's alpha ranging from 0.298 to 0.777. Cronbach's alpha should be viewed with some caution for lower values, especially for scales having only two scale items. Additional evidence of acceptable reliability of the composite constructs was obtained from composite reliability values ranging from 0.724 to 0.881. Overall, the measurement outcomes support the use of the ESG Disclosure Index, but there are a few inconsistencies within the individual parts of the measurement. This measure constraint is taken into account when interpreting the quantitative results.

Ethical principles were adhered to during the study. Responses were anonymous and all respondents provided informed consent prior to the collection of data. The data was anonymized and confidentiality ensured by omitting personal information. All data were used only for academic purposes and kept securely to ensure participants' privacy.

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FINDINGS

The number of SMEs in the study is 156 made up of SMEs in retail, manufacturing and service sector in Blantyre District. This distribution allowed for representation across the three sectors included within the study and enabled interpretation of findings in the context of the urban SME environment of Blantyre District. The companies in the study varied in firm age, firm size, profitability, and prior to the study, access to external funds.

The survey results also showed that many SMEs still had relatively informal management structures. While the majority of the respondents kept basic financial records, few had developed in-depth accounting systems, formal governance or documented sustainability reporting practices. The results confirm earlier research that showed that financial and technical resources are often a limiting factor for SMEs in developing economies to be able to implement more sophisticated reporting methods [12].

Sustainability Reporting Practices

The results reveal that sustainability-related activities were observed in the engaged SMEs, but formal sustainability reporting was still in the fledgling phase. While most respondents said their companies were involved in socially and environmentally good work, they generally reported that the work did not get documented in a structured sustainability report.

The most common sustainability practices reported were:

- Educational initiatives aimed at enhancing the well-being of the community; and
- Employee welfare programs and workplace safety and health;
- Conformance to relevant environmental legislation;
- Ethical business practices; and
- Use of business resources efficiently.

The regretivities reflect that good business conduct is already being practiced in many SMEs, but not necessarily reported in the known sustainability reporting systems, like Global Reporting Initiative (GRI) [4]. In this context, it seems as if there is much more extensive practice of sustainability than sustainability reporting. It is important to note that this distinction is important since lenders can only consider sustainability information that is formally documented and communicated during the credit assessment process. This separation between sustainability practice and sustainability reporting is an important explanation for the lack of a strong quantitative relationship found in this study. An SME can undertake responsible actions like waste minimization, employee wellbeing, involvement in the community, ethical business operations etc. without having to submit a structured ESG report. To a financial institution, an individual's credit history might therefore not be that easy to factor into a formal credit grading system or to see at a glance. The results indicate that the financing potential of sustainability may not only be tied to responsible practices when undertaken by SMEs, but also to their capacity to document, organize and communicate sustainability information that can be understood and utilized by lenders. This could be part of the reason why the qualitative results found value in transparency and the quantitative results did not demonstrate a statistically significant correlation between ESG reporting and access to finance.

Access to Finance

The role of the SMEs in economic development was crucial but many of the participants SMEs still faced severe difficulties in accessing formal finance. Financial records, credit history, having a lack of documentation of your business, and collateral were the main obstacles respondents listed when it came to lending.

The qualitative results showed that there are definite differences in institutional approaches for evaluating SME creditworthiness. The lending process was said to be more formal and structured at NBS Bank, with financial statements and profitability being more important and the ability to pay back and collateral being emphasized. However, PolyMed SACCO had a different approach, as it was a more relationship-based approach that took much more account of member behavior, savings habits, repayment frequency and existing relationships with the institution. This institutional gap should be taken into account when considering the quantitative result that there is no statistically significant overall relationship between ESG-related reporting and access to finance. It implies that the value of sustainability information could be related to, among other things, the priorities of financial institution information and their lending. The differences however, are not interpreted as representing a statistically significant difference between the ESG-finance relationship between NBS Bank and PolyMed SACCO, since the available quantitative results do not allow for regression estimates to be available at the institutional level [1] .

Pearson correlation analysis was conducted on the association of the quantitative variables related to the environmental, social and governance (ESG) reporting and access to finance. There was no statistically significant relationship reported with SME loans access and SME reporting standard adoption ($r = 0.112$, $p = 0.164$), SME loans approval and ESG ($r = 0.000$, $p = 0.997$), social and environmental determinants ($r = 0.108$, $p = 0.179$), ESG regulatory environment in Malawi ($r = 0.124$, $p = 0.123$), ESG compliance and awareness of sustainability ($r = 0.056$, $p = 0.486$). The results suggest that in the sample of SMEs, none of the ESG-related variables measured were significantly related to access to finance. The results, however, must be interpreted as evidence collected from these sampled companies and not as evidence that there is no link between sustainability reporting and the financing of SMEs in other settings.

Results of hypothesis testing were not statistically significant enough to support the proposed relationships. H1 was not supported due to the lack of statistical significance between the ESG-related measure applied to loan approval and the access to SME loans ($r = 0.000$, $p = 0.997$). The social and environmental determinants was not associated with SME loan access ($r = 0.108$, $p = 0.179$) and thus H2 was not supported. The findings of the quantitative results did not show any statistically significant difference in the relationship between ESG and finance in NBS bank and PolyMed SACCO for H3. The qualitative results did, however, reveal a disparity in the institutional lending practices, with NBS Bank focusing more on formal financial documentation and formal credit assessment, and PolyMed SACCO more on the relationship-based information, saving habits, and repayment histories.

Qualitative Findings

The qualitative results added to the quantitative results, providing an understanding of the role financial institutions play in creditworthiness assessment when considering information on sustainability. Four main themes emerged from the thematic analysis.

Theme 1: Traditional financial information continues to be key to making lending decisions.

Conventional financial information consistently remained the basis of the credit assessment of SMEs according to loan officers and managers. The main factors that were identified as determinant of the lending decision were business cash flows, profitability, repayment capacity, financial statements, existing liabilities, and credit history. Sustainability reporting was mostly considered to be supplementary information and not a mandatory loan requirement.

Theme 2: This theme highlights the importance of the initiative of Sustainability Reporting as a tool to increase transparency and credibility of managers.

While sustainability reporting was not considered to be a key consideration to influence loan decision-making, respondents noted that it was a helpful side piece of information for understanding management, governance, transparency and the sustainability of business operations. Participants stated that they would like sustainability information to give lending confidence, especially when existing financial information was not enough to assess borrower quality.

Theme 3: Institutional differences in lending approaches and the use of sustainability information

The qualitative results showed that there was difference in the lending approach of NBS Bank and PolyMed SACCO. NBS Bank had a more formal credit assessment process, focusing on financial documentation and structured risk assessment. On the other hand, the focus of PolyMed SACCO seemed to be more on the members' relationship factors such as members' saving habits, repayment, borrowers' familiarity and community trust.

The differences are helpful to understand the context of how sustainability-related information might be perceived in each institution. Sustainability information could, in a more documentation-based lending process, complement other documentation related to sustainability management, sustainability governance and sustainability long-term business risks. If, however, credit is based on relationships, then borrowers' history, trust, and repayment habits can often be the source of much of the non-financial information needed to assess their creditworthiness.

However, after conducting quantitative analysis, no statistically significant difference was found in the relationship between ESG disclosure and financing outcomes between NBS Bank and PolyMed SACCO. Hence the results should not be viewed as evidence that sustainability reporting had a markedly different financial impact on one institution than on the other but rather as evidence for the institutional approaches to lending.

Theme 4: Small and medium-sized enterprises' limited capacity hinders sustainability reporting

The participants noted various factors that hinder formal sustainability reporting by SMEs. These ranged from limited awareness of ESG reporting frameworks, to weak accounting systems, weak record keeping practices, a lack of technical expertise and the perceived cost of preparing sustainability reporting. They also highlighted the need for institutional support, a streamlined reporting process and specific capacity-building programs, involving SME support organizations, government bodies and financial institutions, to encourage SMEs to adopt sustainability reporting.

DISCUSSIONS

The study analyzed if sustainability reporting benefits SMEs' financing access in Malawi based on some evidence gathered from NBS Bank and PolyMed SACCO in Blantyre District. The study combines the quantitative and qualitative results, giving a complete picture of the importance of Environmental, Social and Governance (ESG) disclosure in the new financial world where lending decisions are still mostly based on traditional financial indicators. The quantitative analysis revealed no statistically significant direct link between sustainability reporting and financing results, but the qualitative evidence indicates that sustainability information can help to increase transparency and provide more information about the quality of the business to lenders.

Sustainability Reporting Among SMEs

The results showed that although SMEs have many good intentions with regard to their environmentally and socially responsible business practices, there isn't much of a formal sustainability report. A majority of the enterprises reported various activities related to participating in the community, caring for employees, using resources efficiently, complying with environmental laws and regulations, and ensuring ethical behavior in business. These practices, however, were not well recorded through the use of widely established sustainability reporting frameworks.

The results of this study are similar to those of earlier studies which indicated that SMEs tend to engage in sustainable practices informally due to financial constraints, lack of technical skills or lack of reporting obligations [14]. SMEs often focus more on day to day business management and survival of the business as compared to formal disclosure of sustainability. As a result, there is a significant divide between the implementation of sustainability practices and systematic reporting.

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An important finding of the study is that there are gaps between sustainable practices and formal reporting. The findings indicate that activities linked to environmental responsibility, employee welfare and ethical business conduct and community engagement are being carried out by some SMEs, but these activities are not necessarily reflected in structured, consistent and externally communicable sustainability disclosures. This is significant as non-formal sustainability practices could not be easily seen by external actors such as lenders. As a result, the information that can be gained from activities undertaken by SMEs in relation to sustainability may not be fully utilized to support credit assessments.

The results are thus a potential explanation for why there was not a statistically significant association between ESG disclosure and financing outcomes studied in this paper. Sustainability-related information may need to be well documented and communicated in a way that is easily understood by lenders, in order for it to influence lending decisions. If this information is not formal, presented in a piecemeal manner or it has not been utilized via the formal reporting mechanisms, financial institutions may have limited capacity to systematically factor this information into credit decisions, including the conditions of a loan. Sustainability may thus not only be a matter of whether SMEs adopt sustainable practices, but also how they can be communicated in a credible and usable way to financial institutions.

The study also found that many of the SME owners still see sustainability reporting as a regulatory/compliance issue rather than a management tool to build stakeholder confidence. This perception might restrict the benefits that could result from disclosing ESG information, especially in financial systems, where knowledge of sustainable finance is comparatively low.

Sustainability Reporting and Access to Finance

The quantitative results show that there is no direct statistically significant effect on SMEs access to finances in Malawi by sustainability reporting as it exists now. The results did not significantly link increased ESG disclosure with loan approval, loan size, interest rates or collateral requirements after adjusting for firm-specific characteristics. The results of the study therefore do not support the notion that the reporting of sustainability has an independent positive effect on financing for SMEs in the current lending market.

These results contrast with most of the evidence from developed economies, which has linked higher sustainability performance with a reduction in financing costs, greater access to external capital, and better investor confidence. Lenders in many developed financial markets are increasingly making sustainability performance a part of their credit assessment as they see sustainability as a sign of good risk management and long-term organizational sustainability.

The conflicting results found in this study may instead be due to variations in institutional development. In the financial sector, in Malawi, the most prominent factors influencing lending remain profitability, capacity to repay, availability of financial statements, credit history and availability of collateral. In the present situation, sustainability reporting is therefore not a major criterion for lending decisions, but rather supplementary information.

The results are not to be understood as a sign that sustainability reporting is not valuable. Instead, they believe that the institutional landscape is not fully adapted to incorporating ESG into the assessment of SME credit. The contribution of sustainable finance to the financial landscape in Malawi could grow in importance as sustainable finance develops in the world.

Interpretation through Information Asymmetry Theory

According to Information asymmetry theory, the lender's problem is that they are uncertain due to the fact that the borrower will have more information about their business operations and prospects available to them than the external financier. Sustainability reporting was anticipated to fill this information gap by offering more evidence on the quality of governance, environmental responsibilities and the management of the organization.

These findings support this theoretical view, in part. While ESG disclosure had a modest impact on financing outcomes quantitatively, the interview participants consistently highlighted the role of ESG information for transparency and the value of it for sources of supplementary information on quality and managerial capability of the organization. The qualitative results indicate that there is informational content in sustainability reporting even when it is not yet incorporated into the formal lending process.

The findings thus extend the information asymmetry theory by showing that, in addition to the availability of additional information, the recognition and integration of that information into the credit evaluation frameworks of financial institutions is an important determinant of information asymmetry. Unless information on ESG issues becomes deeply embedded in the practices of the financial sector, its actual impact on financing decisions will likely be restricted.

Interpretation through Signaling Theory

According to signaling theory, organizations make voluntary disclosures of information to convey positive aspects of the organization to external stakeholders and alleviate uncertainty about it. In the context of SME financing, sustainability reporting was likely to indicate good management, good governance and ethical business practices, as well as reduced risk in doing business.

Qualitative results support this expectation to some extent. Loan officers agreed that sustainability reporting could help to build trust in SME management, through responsible leadership, better governance and longer-term strategic planning. But, these signals are already having only a secondary role during credit assessment, as traditional financial indicators still dominate lending decisions.

Based on the findings, therefore, sustainability reporting is essentially a weak signal in the financing landscape for SMEs in Malawi at the time. ESG disclosure is used to communicate positive characteristics of the organization, but it is limited by its signaling power, in that financial institutions have not yet systematically integrated the issue of sustainability into formal lending frameworks.

Interpretation through Stakeholder Theory

The stakeholder theory also states that value can be created for an organization by meeting the expectations of all the stakeholder groups such as employees, customers, communities, regulators, investors, and financial institutions. Sustainability reporting is one such way for organizations to demonstrate their accountability to these stakeholders.

The results are consistent with this theoretical approach. Sustainability reporting has not yet resulted in better financing outcomes, but financial institutions have understood that responsible business practices can offer them valuable information on governance quality, ethical business practices, organizational resilience and long-term management capacity. The results indicate that even though there is no direct financial gain, sustainability reporting helps to gain legitimacy within the organization and increases stakeholder confidence.

However, the importance of sustainability reporting is not only limited to access to funding. The sustainability reporting process can create these broader organizational benefits, which can help contribute to long-term business sustainability, by enhancing transparency, accountability and stakeholder relationships.

Practical Implications

The findings are relevant for the SMEs, financial institutions and the policy-makers in Malawi, and in particular how sustainability-related reporting is slowly evolving and how it could be incorporated into SME finance.

Sustainability reporting should be seen as a strategic investment for SMEs, not just a compliance exercise. Better disclosure of ESG data may not offer any direct benefits in terms of financing, yet it may help build transparency, governance, and readiness for future sustainable finance developments in an organization.

The results may also indicate a way for financial institutions to move toward integrating relevant ESG indicators in SME credit assessment procedures in an incremental manner. Simplifying ESG assessment tools to suit the characteristics of SMEs may offer additional information to lenders without imposing undue reporting burdens on SMEs.

Short-term regulatory action

The results indicate that a more proportionate approach to sustainability reporting might be more suitable than complex reporting requirements for SMEs for policy and regulatory purposes. The Reserve Bank of Malawi, working with the relevant regulatory and professional bodies, could create or encourage the creation of guidance on the sustainability reporting for SMEs and financial institutions that is user-friendly and more efficient. It might be possible to agree on a limited set of material environmental, social and governance indicators that are reasonably measurable by SMEs and that lenders could consistently understand. The guidance could also prompt financial institutions to separate mandatory financial information for the assessment of credit risk from additional information on sustainability that might be useful in understanding the governance and practices of the financial institution, and its non-financial risks. The method would enable Malawi's sustainable finance framework to mature progressively, while not creating an unfair burden on businesses of lower size to adhere to the framework.

Medium-term action for financial institutions

In the medium term, the Reserve Bank of Malawi can promote financial institutions to conduct pilots on applying a selected set of sustainability-related indicators to the assessment of SMEs credit and risk-management processes. Pilot schemes could determine which ESG indicators are useful in the assessment of credit risk in SMEs and whether disclosing information about these indicators will contribute to a better understanding of the operations of SMEs. The outcomes of these pilots may be used to develop guidance for future supervision of the proportionate use of sustainability information in SME finance. Financial institutions may also offer simple guidance to SMEs regarding the kind of sustainability information that is relevant to their credit application, to aid in closing this loop.

CONCLUSION

In this study, the focus was on the link between sustainability reporting and access to finance for SMEs in Malawi, based on the findings of NBS Bank and PolyMed SACCO in Blantyre District. The study employs a convergent parallel mixed-methods research design which brings empirical evidence to the ongoing discussion around Environmental, Social and Governance (ESG) disclosure and SME financing in an emerging economy characterized by a nascent sustainable finance market.

The results highlight that SMEs undertake various kinds of environmental and social responsibility activities but that formal sustainability reporting is still not that common. Most sustainability related activities are done informally and are not documented using a specific sustainability reporting framework. The quantitative analysis revealed that there was no statistical significant link between ESG-related disclosure and access to finance. Therefore, the results do not confirm a link between the practice of ESG disclosure among the sampled SMEs and loan approval, loan size, interest rates or collateral required. Traditional financial factors such as profitability, repayment ability, financial statements, and credit history and collateral remain the primary factors for lending decisions.

The qualitative results, however, show that financial institutions see the sustainability information as a useful supplement to existing information. The information could help to enhance transparency, offer further information on organizational governance and management practices and be used to support the evaluation of borrower risk. The findings thus indicate that sustainability reporting is not yet an integral part of the

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SME lending decisions in the studied institutions and can be more relevant in Malawi as sustainable finance practices and the capacity of the institutions grows.

The study makes both theoretical and practical contributions. Conceptually, it applies the principles of information asymmetry, signaling and stakeholder views to the under-studied realm of SME financing in an emerging economy in Africa. The results indicate that sustainability disclosure's potential information and signaling role does not necessarily lead to better financing results. Whether sustainability information is formally documented, credible and relevant to lenders and integrated in credit assessment processes may be a key factor in its usefulness. This study also provides contextual evidence that the lack of statistically significant relationships between disclosure of ESG information and financing outcomes does not necessarily imply that sustainability information is not relevant when it comes to financing; instead, the financing relevance is likely to depend on the institutional context where the information is produced and scrutinized.

From a practical perspective, the results demonstrate a disconnect between sustainability related activities carried out by SMEs and formal sustainability reporting and the incorporation of this information into lending decisions. This can be overcome only by a coordinated effort between SMEs, the financial institution and the policy makers. SMEs could be provided with easy mechanisms to record relevant ESG practices, and financial institutions could have a framework of guidance to help them identify the non-financial information that might be relevant to SME credit assessment. The process may be facilitated by the development of proportionate reporting guidance, capacity building and the progressive evolution of a sustainable-finance framework that is suitable for the local context, including by policymakers and regulators, such as the Reserve Bank of Malawi. A step-by-step process would give the opportunity to SMEs to formalize their already implemented sustainability practices and to offer financial institutions the chance to evaluate relevant ESG data in addition to credit assessment.

The study shows overall that sustainability reporting is still a nascent option and not yet a fixture in the finance of SMEs in Malawi. The results highlight the need for more robust transition from informal sustainability practices to credible and usable sustainability information, and for traditional financial considerations to continue to play a key role in SME lending. Larger and more geographically diverse samples (rural SMEs, other financial institutions, etc.) could be further used in future research to investigate whether the link between sustainability reporting and access to finance differs along institutional, sectoral, firm-size and geographic dimensions.

LIMITATIONS AND FUTURE RESEARCH

This study, like all empirical studies, has a number of limitations that should be recognized when interpreting the results of this study.

First, the quantitative part of the study was restricted to the SMEs in Blantyre district and the institutional evidence was from NBS Bank and PolyMed SACCO. The results obtained are not necessarily applicable to the SMEs in rural areas or to other regions of Malawi which could have different business structures, access to financial institutions, market conditions, record keeping practices or financing constraints. The study thus does not provide evidence that can be assumed to be universal or automatically drawn to all Malawian SMEs. The study can be further expanded to rural districts and other urban centers to explore whether there is a difference in relationship between the sustainability reporting and access to finance in different geographical contexts.

Secondly, the study failed to perform statistically powered subgroup analyses among institutional type, firm sector and firm size and firm age. The qualitative results suggest that the NBS Bank and PolyMed SACCO make different approaches in the lending of SMEs, however, the quantitative results available do not enable us to reliably estimate whether there is a systematic difference between the two approaches. These potential moderating effects should be tested in future studies using larger samples of the subgroups and quantitative data specific to institutions.

Thirdly, the study only looked at access to finance as the main outcome of sustainability reporting. However, this research did not attempt to capture and analyze other possible organizational benefits such as increased financial returns, improved operating efficiencies, innovation, customer satisfaction, competitive advantage or long-term sustainability of the business. These wider organizational outcomes should therefore be explored in future research to give a fuller picture of the value added by sustainability reporting.

The study should be replicated in other parts of Malawi; incorporate more commercial banks and non-bank financial institutions, and be compared with other developing economies. Further, the research on the effects of the incorporation of ESG principles into official lending practices would provide valuable evidence on the link between the adoption of sustainability information and SME access to finance.

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