The CSR-CFP 'missing' link: complementarity between ESG practices?

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The goal of this research project is to analyze the relationship between corporate social performance (CSP) and corporate financial performance (CFP)

Our methodology relies on an econometric study on matched ESG ratings from the Vigeo database and economic and financial performance data from the Orbis database.

Short literature review on the CSP-CFP link

The empirical link between corporate social performance and corporate financial performance has received considerable attention for 35 years. Yet there is no consensus in the literature on whether CSP leads (or not) to superior CFP, or whether CFP is necessary for CSP.
This element is illustrated in the following table which shows various surveys published since the 1990s on the links between CSP and CFP

Table 1: The links between CSP and CFP

Authors	**Methodology**	**Period**	**Results**
Roman, Hayibor & Agle, (1999)	Survey of 57 studies		positive: 33 negative: 5 neutral: 14
Griffin & Mahon (1997)	62 studies since 1970	1970-1999	positive: 51 negative: 20 Neutral: 9
Pava & Krausz (1996)	21 studies since 1970		positive: 12 negative: 1 neutral: 8
Margolis, Elfenbein &Walsh (2007)	meta-analysis of 167 studies	1972-2007	Weak positive effect Causality from CFP to CSP

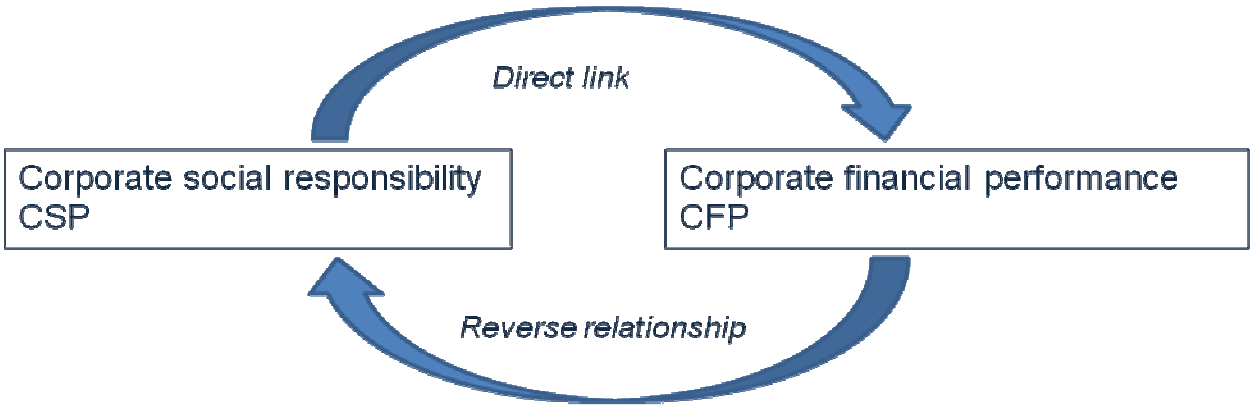
Table 1 (continued): The links between CSP and CFP

Authors	Methodology	Period	Results
Margolis & Walsh (2003)	Survey of 127 studies since 1970	1972-2000	From CSP to CFP Positive: 54 Non significant: 28 Negative: 7 Mixed: 20
			From CFP to CSP Positive: 16 Non significant 3 Mixed: 3
UNEP-Fi et Mercer (2007)	20 studies published in 2000	1972-2004	Positive: 10 Negative: 4 Neutral : 5 Non montonous impact : 1

Recent research points at numerous biases and problems of previous work (eg: Elsayed & Paton. 2005. (Nottingham) or McWilliams and Siegel. (Chicago, NY) 2000) among which: model misspecification (endogeneity), omitted variables in the determinants of profitability; limited data (very small samples , old periods) ; cross-sectional analysis invalid in the presence of significant firm heterogeneity; problems of measurement of CSR; wide diversity of measures used to assess financial performance.

Another problem also lies in the direction and mechanisms of causation, as illustrated in the following figure.

Figure 1: The direction of causality between CSP and CFP



In turn, if there is no consensus on the link between CSR and CFP, this may suggest that it is a specific combination of firm policies that lead to superior performance.

By definition, two or more practices are complements when using one more intensely increases the marginal benefit of using others more intensively (Milgrom & Roberts, 1995). During the 1990s, this argument has proven a useful explanation of the Solow paradox,

wherebv “you can see the computer age except but in the productivity statistics” (Solow, 1987). Indeed, several researchers have shown that only those firms that have adopted both computerization and complementary innovative HRM (human resources management) practices (teamwork, multi-tasking, quality circles etc.) did enjoy superior performance (see e.g. Ichniowski and Shaw 2003; Boucekkine and Crifo, 2008).

By analogy, the apparently ambiguous link between CSP and CFP could presumably be explained by taking into account the complementarity between the multi-dimensional facets of corporate social responsibility.
In fact, a first analysis on the Vigeo database reveals that the distribution of correlation among ESG scores shows strong positive correlations between many ESG policies. This pattern clearly is consistent with the idea that ESG practices are complementary.

This research project will examine how the complementarity between various ESG policies affects corporate financial performance by conducting an econometric study on a matched CSP-CFP database using panel data techniques (in particular the generalized method of moments technique). The database will consist of a matched sample of Vigeo’s ratings together with the economic and financial performance indicators from the Orbis database.

References

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Indicative schedule

Construction of the database : summer 2008- spring 2009.

Econometric estimations : may 2009 – winter 2009.

Presentations at international conferences, diffusion of results, submission for publication: fall 2009- summer 2010.