Rotman
Michael Lee-Chin Family
Institute for Corporate Citizenship

Academic Literature on ESG and Financial Performance

Preliminary Literature Search

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The Michael Lee-Chin Family Institute for Corporate Citizenship at the Rotman School of Management, University of Toronto, helps current and future business leaders integrate sustainability into business strategy and practices.

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Method

A literature search of the academic literature was conducted on ProQuest, using the terms "corporate social performance", "financial performance and social responsibility," and "financial performance and corporate responsibility." To ensure high credibility of papers, only papers cited by over 30 sources are listed; however, recent papers (published since 2010) are exempt from this criteria as they are too new to be cited as frequently. Furthermore, the location is limited to Canada, U.S., and U.K.. Bibliography is organized according to subject categories.

Summary

Meta-Analysis

A majority of meta-analyses point to a positive association between corporate social performance (CSP) and corporate financial performance (CFP). However, there is a general consensus that the relationship is not linear and that its strength is contingent upon various moderators. Moderators discussed in the literature include: environmental performance type (e.g., reactive vs. proactive performance); firm characteristics (e.g., large vs. small firms); methodological issues (e.g., self-report measures vs. third-party audits); company corporate responsibility reputation; structure of the subdiscipline (e.g., accounting vs. social science); executive stakeholder values; and performance maintenance (e.g., short-term vs. long-term). Future research is directed towards uncovering the causal relationship between CSP and CFP, understanding why companies pursue CSP, and the mechanisms that connect CSP and CFP.

Causality

Causal relationship between corporate social responsibility (CSR) and financial performance has been examined via time series approach, which analyzes the long-term, cumulative effect of CSR on financial performance. The findings are inconsistent. Some studies have found that cumulative effects of CSR on firm financial performance strengthen over time (Moore, 2001; Peters & Mullen, 2009), while some have found that the time-lapsed effects are weaker compared to the immediate, short-term effects (Nelling & Webb, 2009), and even null to negative (Makni, Francoeru, Bellavance, 2009; Nelling & Webb, 2009).

Correlations

Majority of the papers on the link between CSP and CFP are correlational in nature. There has been a consistent reporting of positive relationship between CSP and CFP using various statistical methods and in different industries (Friede, Busch, Bassen 2015, among others). Many papers have focused on the moderators that influence this relationship, the most notable of which are: corporate reputation (Neville, Bell, Menguc, 2005), publication outlet (Orlitzky, 2011), CSR engagement strategy (Tang, Hull, & Rothenberg, 2012), firm's level of CSR (McWilliams & Siegel, 2001), R&D investment (McWilliams & Siegel, 2000), age of corporate assets (Cochran & Wood, 1984), and measures of CSR performance (Balabanis, Phillips, Lyall, 1998). There have been few studies that report negative relationship between CSP and CFP (Brammer, Brooks, Paveline, 2006; Cardebat & Sirven, 2010).

Stakeholder Theory

Stakeholder theory is utilized as a framework for investigating and understanding the relationship between CSP and CFP. In other words, stakeholder value and salience are explored as mediators of the CSP-CFP link. Research in this domain focus on the stakeholders' ability to reward or punish the firm based on their evaluations of the firm's social performance and on the firm's ability to meet the demands of multiple stakeholders. An important feature of this argument is that stakeholders underlie the ability to transform social responsibility into profit.

Environment

Papers in this domain have found that firms that engage in corporate environmental responsibility and sustainable practices have higher financial performance compared to those that do not. Some researchers have shown long-term positive effect of sustainable practice (Ameer & Othman, 2012), and others explain that investing in corporate environmental responsibility decreases the firm's environmental costs, which ultimately enhances financial performance (Jo, Kim, Park, 2015).

ESG and Investment Outcomes

Research on financial performance of socially responsible investment, compared to conventional investment (SRI), has yielded largely inconclusive results. Meta-analyses show that the financial performance of SRI changes radically depending on the empirical methodology of the study (Revelli & Viviani, 2013), and that the survivorship bias in a study tended to overestimate the performance of SRI compared to conventional funds (Rathner, 2013).

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Meta-Analysis

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Positive Correlation

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